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ABSTRACT

This instructional guide for an entrepreneurship program of study in secondary schools is a teacher's manual combined with the essential learning activities for students. The 13 units--also appropriate for use at postsecondary or adult levels--may be used as a one-semester course, or in part, or in their entirety as supplements and hands-on experiences to accompany an entrepreneurship text. For each unit these materials are provided: unit objectives, sheets containing necessary content and background information, questions for discussion, transparency masters, and student activities. The 13 units are (1) Introduction to Entrepreneurship and Self-Employment; (2) Selection of Effective Legal Form of Business Organization; (3) Selection of Effective Specialized Assistance; (4) Financing the Small Business; (5) Selecting a Location; (6) Building, Equipment, and Layout; (7) Operating Permits, Licenses, and Tax Regulations; (8) Personnel Management for the Entrepreneur; (9) Building a Flexible Advertising Plan; (10) Determine Pricing and Credit Policies; (11) Inventory and Supplies; (12) Understanding a Basic Accounting System; and (13) Selection of Effective Protective Steps. (YLB)

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PREPARING FOR ENTREPRENEURSHIP

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Kenneth L. Rowe
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INTRODUCTION

An increasing number of textbooks and articles on small business management have been published within the last few years. The popularity of the subject should not be a surprise to teachers who frequently aid students in career planning. In addition to preparing themselves to become productive employees, a number of students are also interested in developing skills that would enable them to become self-employed.

By definition, entrepreneurship is the act of organizing, managing and assuming responsibility for a business or other enterprise. The entrepreneurship program of study, as presented in this instructional guide, has the potential of becoming an added dimension of the existing Vocational Education program. Vocational Education is typically viewed as a program that prepares persons for employment in existing organizations. The entrepreneurship program goes a step further by preparing persons to initiate enterprises thereby creating their own employment opportunities. The net result is that Vocational Education will be involved in job creation as well as occupational preparation.

Scope and Limitations of Project

"Preparing for Entrepreneurship" is an Instructional Guide containing materials for use by both the teacher and student. For each of several essential units of instruction, these materials have been provided:

1. Several clearly stated objectives.
2. Information sheets containing necessary content and background information. These are designed to be primarily utilized by the teacher. However, the materials could also be duplicated and distributed to students.

3. Questions for discussion designed to enhance student interest and involvement.

4. Transparency masters have been provided where it will be necessary for the teacher to present pertinent information and data on an overhead projector.

5. Student activities that will provide students with an opportunity to apply concepts learned in the various units.

Organizational Plan of Project

The typical unit in the instructional guide contains five objectives. For planning purposes, the teacher will find that no more than one objective could be covered in one class period.

The units are designed in such a way that they may be used individually and plugged into any course. They are self contained and not dependent upon the content of any other unit. Since they are not interdependent, the units may be sequenced according to the needs of the class or the wishes of the user.

It should be pointed out that this project is an instructional guide and not a textbook to be used by students. As an instructional guide, the manual provides the teacher with a well-planned approach to be used for incorporating instruction in entrepreneurship into the schools.

It is suggested that teachers use the materials to guide students through the process of learning about entrepreneurship. It could be said that "Preparing for Entrepreneurship" is a teacher's manual combined with the essential learning activities for students.

Purpose of Project

The overall purpose of this project is to present an instructional program to be used in secondary schools for persons who wish to explore and/or prepare for careers in entrepreneurship. (The term "entrepreneurship" used in the materials is synonymous with the term "self employment.") The content is appropriate for careers in any occupational field.

The final product as presented here is an instructional guide designed to assist students in assessing interests and abilities with respect to self employment. The guide contains materials addressing needs of both the instructor and the students.

The units are also appropriate for use at other educational levels -- post secondary or adult. By the uniqueness of their design, whole units or parts of units may be used depending upon the need and intended purpose of the user.

Depending on the level of the learner, the instructor may choose to use the units as supplements and "hands-on" experiences to accompany an entrepreneurship text.

The units were selected on the recommendations of the Advisory Committee and if used as recommended, should fulfill the needs of a one semester course on entrepreneurship.

Human and Fiscal Resources Needed

Key resources needed in implementing the program in a school are:

1. A copy of "Preparing for Entrepreneurship" and the capability of duplicating copies of Student Activities for each student.
2. A teacher interested in preparing students for entrepreneurship and who has a willingness to keep up to date with development in the small business sector of the economy.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

OBJECTIVES

After completing this unit, the student will be able to:

Objective 1.1	Define entrepreneurship and self-employment.
Objective 1.2	Describe the failure rate of new businesses.
Objective 1.3	Identify the questions that must be answered by a feasibility study.
Objective 1.4	Identify some businesses that offer the most promise for the future.
Objective 1.5	Identify some businesses that offer the least promise for the future.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

INFORMATION SHEET

Objective 1.1: Define entrepreneurship and self-employment.

A. Entrepreneurship -- The act of organizing, managing, and assuming responsibility for a business or other enterprise.

B. Entrepreneur (traditional definition) -- A person who starts a new business from scratch to make or sell new products or services. Persons who fit this definition are Henry Ford who started the Ford Motor Company and John D. Rockefeller who founded the Standard Oil Company of Ohio.

C. Entrepreneur (modern definition) -- A person who starts a business, even though the products or services are not new. An example is a person who buys a business that was started by someone else.

D. Self-employment -- Working for oneself, with direct control over work performed and fees to be charged.

E. Small business -- One which is independently owned and managed and not dominant in its field. (Independently owned means that it is not part of another business. Independently managed means the owner should be free to run the business as he or she pleases. Not dominant in its field means the business accounts for only a small part of the total sales volume in its industry.)

F. Small enterprise -- Synonymous with small business and self-employment.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

QUESTIONS FOR DISCUSSION

Objective 1.1: Define entrepreneurship and self-employment.

A. Who are some other persons who meet the traditional definition of entrepreneur?

B. Do you personally know anyone who is an entrepreneur according to the modern definition? Describe that person.

C. When you think of your career, do you see yourself as an employee in a large business or as an entrepreneur? Explain.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

STUDENT ACTIVITIES

Objective 1.1: Define entrepreneurship and self-employment.

1. In the next 10 minutes, list as many different types of small enterprise in your town as you can.

2. When instructed to do so by your teacher, compare your list with those of two or three other students and add any additional enterprises to your list.

3. Of the small enterprises listed, which would you enjoy owning and operating? Place a check mark (✓) next to those you like. Then, in the space below, describe what those enterprises have in common.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

INFORMATION SHEET

Objective 1.2: Describe the failure rate of new businesses.

A. Of the more than 500,000 new businesses formed each year, one-third will end operations by the end of the first year and one-half of the original number will be out of business by the end of the second year. By the end of the fifth year, one-fifth of the businesses will be in existence.

B. Causes of small business failure --

According to Dun and Bradstreet, Inc., the credit reporting company, small businesses fail for the following reasons:

1. Incompetence -- Not qualified or not having the ability to do the job.
2. Unbalanced experience -- Knowledge or experience not well rounded in sales, finance, purchasing, and production.
3. Inexperience in line -- This means that the entrepreneur has some business experience, but not in the particular line of goods or services of the business that failed.
4. Inexperience in management -- Lack of experience in planning, organizing and controlling and in getting work done through other people.
5. Neglect -- Individuals tend to neglect when they either lack motivation or are frustrated with the difficult task of starting a new enterprise.
6. Fraud -- A very small percentage of businesses fail for this reason. Fraud occurs when deceptive and dishonest business practices are used. The business may succeed for a short time, but the fraud is likely to be uncovered in due time.
7. Natural disasters -- Some failures have been caused by floods, tornadoes, and earthquakes.

C. Is the small business sector in poor health?

There is no question that the summary statistics of business failures mask numerous cases of broken dreams and personal financial ruin. It should not be assumed, however, that small business is no longer a viable career option for the future.

Many lines of business are so easy to get into that high failure rates should be expected. Also, numerous small businesses are operated by persons who are not totally committed to making the venture a success.

While specific statistics are not available, it is thought that the business failure rate is abnormally high because of the presence of many owners who are inclined to abandon the business at the first sign of trouble. These persons are not prepared, either financially or psychologically, to stay with the venture through hard times.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

QUESTIONS FOR DISCUSSION

Objective 1.2: Describe the failure rate of new businesses.

A. Why do you think some persons go into business for themselves before they are adequately prepared?

B. Can you give some causes of business failure not mentioned so far in this discussion?

C. Are you familiar with any small enterprises that have gone out of business recently? What types of business was it?

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

STUDENT ACTIVITIES

Objective 1.2: Describe the failure rate of new businesses.

1. In the space provided, list what you think are the advantages and disadvantages of owning your own small business.

SMALL BUSINESS OWNER

ADVANTAGES	DISADVANTAGES

2. In the space provided, list what you think are the advantages and disadvantages of being a salaried employee in a large company.

SALARIED EMPLOYEE

ADVANTAGES	DISADVANTAGES

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

STUDENT ACTIVITIES (Con't)

Objective 1.2: Describe the failure rate of new businesses.

3. Inexperience in management is one of the causes of small business failure. If you decide to start your own business, describe how you will gain management experience before launching the business.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

INFORMATION SHEET

Objective 1.3: Identify the questions that must be answered by a feasibility study.

A. Most persons who start a business have not started one before. It is important, therefore, that they understand the size of the task. One of the best ways to do this is through a feasibility study. In short, a feasibility study requries that you look at your prospective enterprise in light of your personal qualities and interests. Seven key questions comprise the basis of the study:

1. What specific skills are required for success in the business I have selected?

2. Do I possess the required skills, or should I team up with a partner who has the skills?

3. Do I have a feasible business idea?

4. Do others, especially experts in the field, believe it is feasible?

5. Do I have access to appropriate financing that will keep the business going until it produces a profit?

6. When will business proceeds be sufficient for supporting me and my family?

7. What do members of my family think about the proposed business venture?

B. Having completed the feasibility study, if you are still interested in starting your own enterprise, you should begin work on a business plan. A business plan is a written document used in acquiring capital for a business. Key items included in the plan are:

1. A description of the business to be organized, including a discussion of how the new business will compare with existing competition.

2. An outline of realistic goals for the business.

3. An outline of the strategy to be used in reaching the goals. (For example, if the first year sales goal is $85,000, how is the inventory needed for that level of sales going to be financed?)

4. A description of the personal qualifications of all key personnel in the business. (Emphasis is placed on how background and experience are related to the enterprise.)

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

QUESTIONS FOR DISCUSSION

Objective 1.3: Identify the questions that must be answered by a feasibility study.

A. What skills must a person possess if he or she desires to start a new business?

B. How can you find out if you really have what it takes to start your own business?

C. What is a business plan? How does the business plan differ from the feasibility study?

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UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

STUDENT ACTIVITIES

Objective 1.3: Identify the questions that must be answered by a feasibility study.

1. What business do you want to enter?

2. What products or services will you sell? (Be specific. If you are interested in opening a restaurant, identify the main menu items you will feature.)

3. Why will customers want to buy your product or service? (In answering this question, describe what you are trying to do better or differently from your competitors.)

STUDENT ACTIVITIES (Con't)

Objective 1.3: Identify the questions that must be answered by a feasibility study.

4. Have three other students read your answers to Parts 1, 2, and 3 and ask them to give their reaction to your idea for a new business. Write a summary of their comments in the spaces below.

Student #1: ______________________________

____

____

____

Student #2: ______________________________

____

____

____

Student #3: ______________________________

____

____

____

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

INFORMATION SHEET

Objective 1.4: Identify some businesses that offer the most promise for the future.

A. According to a survey conducted by a national magazine,* the ten small businesses most likely to succeed are:

1. Building materials store -- Many consumers are spending evenings and weekends on do-it-yourself repairs.
2. Auto tire and accessories -- Many motorists have the knowledge, skill, and interest to perform their own auto repairs. In addition, it is a hobby for many.
3. Liquor stores -- This industry has shown strong growth in recent years.
4. Sports and recreation clubs -- The growing interest in physical fitness has increased the popularity of these clubs.
5. Funeral homes and crematories -- As a business, this is often overlooked by many entrepreneurs. The increasing size of the senior citizen population means an increase in the need for these services.
6. Seed and garden supply stores -- There is currently a high level of interest on the part of consumers in planting home vegetable gardens and ornamental plants.
7. Sporting good manufacturers -- Bicycling, camping, snow and water skiing, and team sports are more popular than ever. Manufacturers of equipment for the activities are experiencing growth rates that are higher than average.
8. Engineering, laboratory, and scientific equipment -- Research being conducted in industry, particularly in aerospace and pollution control, has created this demand.
9. Hardware stores -- Increased consumer interest in do-it-yourself repairs benefits hardware stores.
10. Office supplies and equipment -- Many businesses in this industry have had profitable years in recession periods apparently because their customers (i.e., other business firms) always need office supplies.

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*Marlys Harris, "The Entrepreneurs: Do You Have What It Takes?" Money, March 1978, Vol. 7, pp. 49-54.

B. By the year 2000, some industries will profit from trends in affluence and leisure, urbanization, and technology.

1. Affluence and leisure time -- As consumers have more money to spend and more leisure time, they are likely to be in the market for services related to recreation, travel, banking, and real estate.

2. Urbanization -- Certain industries are likely to benefit from the concentration of persons living in urban areas. These are day-care nurseries, housing construction, and equipment rental.

3. Technology -- The vast number of appliances and technical products used in home and business will require service businesses to handle repairs.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

QUESTIONS FOR DISCUSSION

Objective 1.4: Identify some businesses that offer the most promise for the future.

A. More and more women with small children are holding full-time jobs. Can you think of a business you could start to serve the needs of working mothers? Explain.

B. Which businesses surprised you most by being listed in the top ten best and most likely to succeed list? Why?

C. The "ten best" list suggests that consumers are interested in do-it-yourself repairs. Can you think of do-it-yourself repair businesses not mentioned?

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

STUDENT ACTIVITIES

Objective 1.4: Identify some businesses that offer the most promise for the future.

1. Pick one of the "ten best" small businesses in which you have a particular interest. Write a short report by answering the following questions:
   - (a) How many businesses of this type exist in your community?
   - (b) What is the average length of time these businesses have been in operation?
   - (c) To what do you attribute the success of this type of business?
2. Visit the owner of one of the "ten best" types of businesses in your community. Ask the following questions of the owner, and compare responses received with those of classmates.
   - (a) To what does the owner attribute the success of the business?
   - (b) What annual growth (i.e., percent) has this business experienced since "day one" of operation?
   - (c) Roughly, how much profit did this business make for each dollar of sales in year 1? In the last fiscal year?

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

INFORMATION SHEET

Objective 1.5: Identify some businesses that offer the least promise for the future.

A. According to the survey mentioned earlier, the ten small businesses most likely to fail are:

1. Local laundries and dry cleaners -- Consumers are increasingly using home laundry equipment and synthetic fabrics.
2. Used-car dealerships -- Consumer interest in used cars is dwindling. Because business is slow, banks are generally shying away from making loans to used-car dealers.
3. Gas stations -- Franchises are faced with stiff competition and decreased profit margins. Self-service, full service, specialty fix-its, etc. are currently being offered to draw customers.
4. Local trucking firms -- Union demands and government regulation make this a risky business.
5. Restaurants -- Poor management is the major cause of restaurant failure. Location is also important. Franchises which offer management assistance, reputation, and economies of scale do best but require a large cash investment from the prospective entrepreneur.
6. Infants' clothing stores -- Small retail clothing stores in general are faced with rough competition. Infants' clothing stores in particular face decreased demand since babies are currently not booming.
7. Bakeries -- Supermarket bakery departments offer stiff competition to small, independent store owners. Location is important. Also, offering specialized services increases chance of success.
8. Machine shops -- This business is highly competitive.
9. Grocery and meat stores -- Small grocery store owners face low profit margins, high initial investment, and much competition. Stores which offer special services (e.g., delivery) do the best.
10. Car washes -- Stiff competition, high turnover, and high initial investment make this an unattractive business.

B. Some industries will be adversely affected by environmental trends. See Part B of the Objective 1.4 Information Sheet for a discussion of trends in affluence and leisure, urbanization, and technology.

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

QUESTIONS FOR DISCUSSION

Objective 1.5: Identify some businesses that offer the least promise for the future.

A. Which businesses surprised you most by being listed in the top ten worst and least likely to succeed list? Why?

B. The "ten worst" list suggests that competition is a major factor in determining business success or failure. Can you think of businesses not mentioned which face stiff competition? What special products or services might these businesses offer to differentiate themselves from competition?

C. What restaurant franchises exist in your community? Which seen the most successful to you? Why?

UNIT 1.0

INTRODUCTION TO ENTREPRENEURSHIP AND SELF-EMPLOYMENT

STUDENT ACTIVITIES

Objective 1.5: Identify some businesses that offer the least promise for the future.

1. Select one of the "ten worst" small businesses in which you have a particular interest. Write a short report by answering the following questions:
    (a) How many businesses of this type exist in your community?
    (b) In general, have these businesses been in operation over five years?
    (c) What problems and opportunities exist with this type of business?

2. Visit a successful owner of one of the "ten worst" types of businesses in your community. Ask the following questions of the owner, and compare responses with classmates.
    (a) What problems and opportunities are peculiar to this business?
    (b) To what does the owner attribute the success of the business?
    (c) What annual growth (i.e., percent) has this business experienced since "day one" of operation?
    (d) Roughly, how much profit did this business make for each dollar of sales in year 1? In the last fiscal year?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

OBJECTIVES

After completing this unit, the student will be able to:

Objective 2.1	Describe characteristics of the proprietorship and determine advantages and disadvantages this legal form of business organization can provide.
Objective 2.2	Describe characteristics of the partnership and determine advantages and disadvantages this legal form of business organization can provide.
Objective 2.3	Describe characteristics of the corporation and determine advantages and disadvantaves this legal form of business organization can provide.
Objective 2.4	Determine and discuss decision factors affecting the selection of an effective legal form of business organization.

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

INFORMATION SHEET

Objective 2.1: Describe characteristics of the proprietorship and determine advantages and disadvantages this legal form of business organization can provide.

A. An individual or sole proprietorship is a business, whether large or small, owned by only one person. Proprietorships exist in every line of business but are most numerous in agriculture, in retail stores, and in services such as laundries and repair shops because these fields require relatively little money and few employees to start up. Generally, proprietorships are small enterprises, and they show comparatively small profits as a group. This form of legal organization continues to be very popular in the United States, however, because many people want to have their own business, because it is the form most closely associated with the values of hard work and self-reliance, and because of the ease in starting a proprietorship.

B. Sole proprietorships, although generally small, present several advantages. Some advantages are as follows:

1. Easily formed and terminated. Some licensing and restrictions are necessary, but the sole proprietorship can be formed without many formalities. Essentially, a proprietorship is created when an individual simply starts doing business. The proprietorship can also be easily terminated through sale.

2. Direct, undiluted management and control. Sole proprietors are free, within restrictions of the law, to do as they please without consulting anyone. Proprietors can make their own decisions regarding such things as when to go into business, when to expand, when to shut down, what hours to keep, what prices to charge, and whom to hire.

3. All profits to the owner. No one else shares in the profits ultimately available to proprietors. They work for themselves, determine their own destiny, and can easily see how well they are doing.

4. Flexibility. Proprietors are able to act quickly regarding necessary changes in their businesses since they need consult no one.

5. Secrecy. Generally, sole proprietors need reveal operating plans and profits to no one.

6. Minimum taxation and regulation. Although large proprietorships often incorporate for tax reasons, small proprietorships have a theoretical tax advantage since proprietors pay taxes only on personal income they earn from their businesses. Because proprietorships are generally small and lack economic power, they have not been the focus of much regulation and special tax treatment.

C. Before adopting this form of business organization, consideration should be given to whether advantages outweigh disadvantages for a particular business. Some disadvantages associated with sole proprietorships are as follows:

1. Management limitations. The prosperity of the proprietorship depends on the time and talents of one person. If the proprietor's talents are limited, absence of exchange of opinion before decision making can lead to poor management. Sole proprietors are frequently emotionally unwilling and financially unable to seek outside assistance. Even when proprietors are willing and able to hire outside help, they are often unwilling to share managerial responsibilities. Without such responsibilities and without the incentive of ownership, capable outsiders tend to stay with the business only a short time.

2. Unlimited liability. The business and the owner have no separate legal existence. Proprietors must, therefore, be prepared to satisfy any damages or debts that can be attributed to their businesses with their own personal assets. For example, if a proprietor's truck were to injure people, the resulting obligation might not only end the business but might also personally bankrupt and impoverish the owner for years.

3. Limited fund raising. Capital is generally limited to the owner's personal assets and ability to borrow. Small proprietorships often have greater difficulty borrowing money from banks and frequently pay higher interest rates to get the money than do corporations that are regular bank customers and that are considered safer credit risks. Growth and expansion in small proprietorships can, therefore, be seriously restricted.

4. Limited life. The life of a proprietorship is limited by the life of the owner or the owner's ability to sell the business. Generally, a proprietorship will not outlive an owner unless arrangements have been made to form a partnership, to form a corporation, or to merge with a larger existing company.

Discussion Overhead for Objectives 2.1, 2.2, and 2.3

Advantages and Disadvantages of Selected Legal Forms of Business Organization

Form of Organization	Advantages	Disadvantages
Sole Proprietorship	Easily formed and terminated Direct, undiluted management and control All profits to owner Flexibility Secrecy Minimum taxation and regulation	Management limitations Unlimited liability of owners Limited fund raising ability Limited life of the business
Partnership	Easily formed Combined resources Fund raising ability Management and profit incentive Minimum taxation and regulation	Unlimited liability of owners Management conflicts Limited life of the business Difficult transfer of ownership
Corporation	Limited liability of owners Unlimited life of the business Easy transfer of ownership Fund raising ability Managerial talent	Complicated formation Heavy taxation and regulation Division of owners and managers Unlimited liability for small corporations Business in other states

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

QUESTIONS FOR DISCUSSION

Objective 2.1: Describe characteristics of the proprietorship and determine advantages and disadvantages this legal form of business organization can provide.

A. What are characteristics of a sole proprietorship?

B. Why are proprietorships popular in the United States as a legal form of business organization?

C. In what fields are proprietorships most numerous, and why? What fields are unsuitable for proprietorships, and why?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

QUESTIONS FOR DISCUSSION (Con't)

Objective 2.1: Describe characteristics of the proprietorship and determine advantages and disadvantages this legal form of business organization can provide.

D. What are some of the advantages the sole proprietorship legal form of business organization can provide a small business (see Discussion Overhead for Objectives 2.1, 2.2, and 2.3)?

E. What are some of the disadvantages associated with the proprietorship as a legal form of business organization (see Discussion Overhead for Objectives 2.1, 2.2, and 2.3)?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES

Objective 2.1: Describe characteristics of the proprietorship and determine advantages and disadvantages this legal form of business organization can provide.

1. List advantages and disadvantages that you think a sole proprietorship provides a small business.

SOLE PROPRIETORSHIP

ADVANTAGES	DISADVANTAGES

2. List the name, the size and type of business, and the location of as many sole proprietorships as you can think of in your community.

3. Requirements for forming a sole proprietorship vary somewhat from community to community. What are the requirements in your city?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES (Con't)

Objective 2.1: Describe characteristics of the proprietorship and determine advantages and disadvantages this legal form of business organization can provide.

4. Visit a local sole proprietorship and ask the owner strengths and weaknesses this legal form of organization presents his/her special business. Why does he or she favor the sole proprietorship form of business organization?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

INFORMATION SHEET

Objective 2.2: Describe characteristics of the partnership and determine advantages and disadvantages this legal form of business organization can provide.

A. A partnership is the legal association formed when two or more individuals agree to start a business enterprise as co-owners. Partnerships are an especially popular form of business organization in professional and financial service fields. A partnership can range in size from large law firms with hundreds of partners and thousands of employees to two-chair beauty shops with no employees. Like proprietorships, however, partnerships tend to be generally small enterprises and to show relatively weak profits as a group. Although partnerships are important because they exist in indispensable service businesses, fewer partnerships exist than do other forms of legal business organization.

B. Partnerships present several advantages. Advantages include the following:

1. Easily formed. Unlike sole proprietorships, partnerships are formed under state laws. Laws for forming, maintaining, and dissolving them are usually simple, however, and a general partnership can be formed without many formalities. To form a partnership, each partner customarily contributes economic assets such as money, property, skill, or labor to the business. A written statement between partners is not necessary, although a written partnership agreement specifying the partnership's purpose, assets each partner brings to the firm, work for which each partner is responsible, and the percentage of each partner's interest in the firm is desirable.

2. Combined resources. Partnerships are often useful in combining two or more persons who have more business potential as a group than as individuals. Combining ideas, managerial talent, money and fixed assets can frequently increase a firm's ability to create wealth.

3. Fund raising. Partnerships can generally raise money needed to do business more easily than can sole proprietorships since the financial resources of all the general partners support negotiations for business capital.

4. Management and profit incentive. Partners have a direct voice in management of the firm as compared with corporate employees. Knowledge that the success of the business depends in part on each partner's efforts and that each partner will be rewarded as agreed upon in the partnership agreement as business prospers serves as motivation to partners. Also, motivation to employees might include the chance to become a partner.

5. Minimum taxation and regulation. Like proprietorships, small partnerships have a theoretical tax advantage since business income is taxed only as personal income of each partner. Partnerships have also not been subjected to much regulation.

C. Given these advantages, why do fewer partnerships exist than do other forms of legal business organization? Disadvantages associated with general partnerships are as follows:

1. Unlimited liability. All partners in a general partnership are liable for the actions of each other even though they may be unaware of the actions of other partners. Partners must, therefore, be prepared to satisfy any court damages or debts that can be attributed to their businesses to the full extent of their personal fortunes. The size of partnerships, as a result, is often limited.

2. Management conflicts. Each partner has power to make decisions since management and control is usually equally vested in partners. A mistake by one partner affects all partners. Disagreement may affect business adversely and may even wreck the partnership. Also, a practical limit exists to the number of managing partners desirable since exchange of opinion gets more complicated as more partners are added.

3. Limited life. Long-term growth of partnerships is often prevented since partnerships customarily are liquidated and die with the death of a partner. As with the sole proprietorship, however, arrangements can be made to provide for the firm's survival after the death of the partners.

4. Difficult transfer of ownership. Partners may have difficulty withdrawing from a partnership should they become dissatisfied with the business. Transfer of ownership is by mutual agreement of the partners, and the value of one partner's share of the business is often not easily determined.

D. It should be noted that it is possible to organize various types of partnerships.

1. General vs. limited partners. General partners perform all the functions of the partnership, are usually entitled to large shares of the profits of the business, and have unlimited personal liability as mentioned above. Limited partners bring money into the partnership, have no voice in the management of the business,

receive a share of the profits of the business in return for their investment, and are liable only for the amount of their investment. Both general and limited partners must exist in a limited partnership arrangement. Partners should consult an attorney before forming a limited partnership to discuss in detail whether this legal form of business organization is more appropriate than one of the other forms.

2. Senior vs. junior partners. Senior partners are managing partners who make all the decisions for the firm. Junior partners buy shares in the firm in exchange for part of the profits of the firm.

3. Silent partners. Silent partners have no voice in day-to-day management decisions. They perform special tasks for the firm and share in the profits. Silent partners may be general or limited partners and may be senior or junior partners.

4. Nominal partners. Nominal partners may be general or limited, senior or junior partners. They are usually famous persons who lend their names to the partnership, have no interest in the workings of the firm, and share in the profits in exchange for use of their names.

5. Secret partners. Secret partners may be general or limited, senior or junior partners. They are unknown to the public and are usually active in the business.

6. Dormant or sleeping partners. Dormant partners are often limited partners and may be junior or senior partners. They are unknown to the public, are not active in the firm, provide the partnership with capital or other tangible assets, and share in the profits.

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

QUESTIONS FOR DISCUSSION

Objective 2.2: Describe characteristics of the partnership and determine advantages and disadvantages this legal form of business organization can provide.

A. What are characteristics of a partnership?

B. What various types of partnerships are possible to organize? Briefly, what are the characteristics of each?

C. In what fields are partnerships especially popular?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

QUESTIONS FOR DISCUSSION (Con't)

Objective 2.2: Describe characteristics of the partnership and determine advantages and disadvantages this legal form of business organization can provide.

D. What information is typically included in a partnership agreement?

E. What are some of the advantages the partnership legal form of business organization can provide a small business (see Discussion Overhead for Objectives 2.1, 2.2, and 2.3)?

F. What are possible reasons that fewer partnerships exist than do other forms of legal business organization (see Discussion Overhead for Objectives 2.1, 2.2, and 2.3)?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES

Objective 2.2: Describe characteristics of the partnership and determine advantages and disadvantages this legal form of business organization can provide.

1. List advantages and disadvantages that you think a general partnership provides a small business.

GENERAL PARTNERSHIP

ADVANTAGES	DISADVANTAGES

2. List the name, the size and type of business, and the location of as many partnerships as you can think of in your community.

3. Requirements for forming a partnership vary somewhat from place to place. What are the requirements in your community?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES (Con't)

Objective 2.2: Describe characteristics of the partnership and determine advantages and disadvantages this legal form of business organization can provide.

4. Visit a local partnership and ask one of the partners strengths and weaknesses this legal form of organization presents his/her particular business. Why does he or she favor a partnership? What types of partners are involved in this partnership?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

INFORMATION SHEET

Objective 2.3: Describe characteristics of the corporation and determine advantages and disadvantages this legal form of business organization can provide.

A. A corporation is a legal entity authorized to act as a private person and is considered separate and distinct from the persons who are its owners. These "artificial persons" have unlimited life spans, are empowered by the state to carry on specific business, are owned by shareholders who are liable only to the extent of their investment, and are permitted to own property, to sue and be sued, and to make business contracts. Considerably fewer corporations exist in the United States than do sole proprietorships. The corporate form of ownership, however, has by far the greatest impact in the country in terms of money, size, and power.

1. Formation. To form a corporation, three or more persons assume the role of incorporators. They supervise the organization of the corporation and act as officers until a board of directors and officers are elected. Incorporators usually hire a corporate law specialist to help them draw up a corporate charter which every state requires. A corporate charter includes general purposes of the corporation, identification information, provision for stock, provision for officers and directors, and means for establishing and amending by-laws. By-laws gives rules for a corporation's day-to-day business conduct and include powers of officers, time and place of stockholders' and directors' meetings, and directors' fees. The charter is sent to the state's secretary of state for approval. The corporation, once the charter has been approved, has a permanent life that can be ended only by violation of the charter or by the stockholders.

2. Stock. Ownership of a corporation is held by a group of individuals who buy shares of stock in the corporation. The corporate charter specifies the number of shares of stock the corporation is to have, the classes of stock along with the rights represented by each class, the par value (i.e., stated value at the time of issuance), and the number of stockholders' meetings per year.

   Two classes of stock may typically be issued: common stock and preferred stock. Common stock is most often issued. It includes voting rights and provides unguaranteed and variable dividends (i.e., payments to shareholders). Preferred stock generally does not include voting rights and pays guaranteed fixed dividends.

3. Organization. A separation of roles exists in the corporate form of legal organization. The stockholders are the owners, and common stockholders are theoretically the ultimate governing body of the corporation. Stockholders receive regular reports from management on the firm's operations. The stockholders form too large and too dispersed a group to manage their business effectively, however. The board of directors, therefore, exercises control over the corporation. The board is responsible for forming general policies, for approving important operating decisions such as whether to build a new factory or whether to develop a new product line, and for election of officers. The president and executive officers manage the corporation.

B. The corporate form of legal organization provides a number of advantages not provided by sole proprietorships or partnerships. Some advantages provided are as follows:

1. Limited liability. The liability of stockholders is limited to the amount of their investment in the corporation's stock. Owners' entire personal fortunes, therefore, are not placed in jeopardy.

2. Unlimited life. The corporation can continue indefinitely since it need not be liquidated when a stockholder dies. The length of life of a corporation depends on the corporate charter and business success combined with stockholders' wishes.

3. Transfer of ownership. Stockholders can easily withdraw from a corporation by selling stock to someone else. Business functions and other stockholders are not directly affected. Problems may arise in finding a market to buy stock, but this is typically only in a small corporation.

4. Fund raising. Corporations can generally raise larger sums of money for business operations than can either sole proprietorships or partnerships. This makes large-scale operations possible.

5. Managerial talent. The corporation is often able to obtain managerial talent and specialized skills easier than sole proprietorships or partnerships since assemblying large amounts of economic resources is relatively easy.

C. Although no other form of legal organization has been as successful in the United States as the corporation in bringing together money, resources, and talent and in creating wealth, disadvantages exist to incorporating. Disadvantages are as follows:

1. Complicated to form. Creating a corporation requires considerable time and effort. Also, charter fees and legal fees may make incorporating prohibitively expensive for small firms.

2. Heavy taxation and regulation. The corporation is subject to considerably more control and more exacting compliance with regulations than are sole proprietorships or partnerships. As a result, the officers and managers must keep more formal records and must publish financial information. Also, small corporations are taxed more heavily than are small sole proprietorships or partnerships. All corporations pay corporate income tax; and shareholders, who may be family members in a small corporation, must pay income taxes on salaries and dividends received.

3. Possible division of owners and managers. Where ownership and management are separated, a possibility exists for irregularities, fraud, and laxity on the part of both owners and managers.

4. Unlimited liability for small corporations. A bank may require the principal owners of a small corporation to personally endorse a loan. Such an endorsement negates the limited liability advantage of the corporate form of organization since the bank has a claim on the personal assets of the endorsers of the loan should the corporation be unable to repay the loan.

5. Doing business in other states. To transact business in another state, a corporation usually has to file a copy of its charter in that state.

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

QUESTIONS FOR DISCUSSION

Objective 2.3: Describe characteristics of the corporation and determine advantages and disadvantages this legal form of business organization can provide.

A. What are characteristics of a corporation?

B. How are corporations formed? How are they dissolved?

C. What are two classes of stock that may be issued by a corporation? Which class of stock pays guaranteed fixed dividends?

QUESTIONS FOR DISCUSSION (Con't)

Objective 2.3: Describe characteristics of the corporation and determine advantages and disadvantages this legal form of business organization can provide.

D. Who owns, who exercises control over, and who manages a corporation?

E. What advantages are provided by the corporate form of legal business organization (see Discussion Overhead for Objectives 2.1, 2.2, and 2.3)?

F. What are disadvantages that exist to incorporating (see Discussion Overhead for Objectives 2.1, 2.2, and 2.3)?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES

Objective 2.3: Describe characteristics of the corporation and determine advantages and disadvantages this legal form of business organization can provide.

1. List advantages and disadvantages that you think a corporation provides a small business.

CORPORATION

ADVANTAGES	DISADVANTAGES

2. List the name, the size and type of business, and the location of as many corporations as you can think of in your community.

3. Determine requirements for a business to incorporate in your state. Must any additional city or county regulations be met?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES (Con't)

Objective 2.3: Describe characteristics of the corporation and determine advantages and disadvantages this legal form of business organization can provide.

4. Visit a local corporation and ask one of the officers why the corporate form of business organization is favored for this particular business. Ask if you can see a share of stock.

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

INFORMATION SHEET

Objective 2.4: Determine and discuss decision factors affecting the selection of an effective legal form of business organization.

A. Prior to weighing pros and cons of various legal forms of business organization and selecting an appropriate form, prospective owners must consider a number of factors that are important to this decision. Typically, a list of such factors includes the following:

1. Ease of formation. How much time, effort, and money are available to start up the business?

2. Length of life of the business. Is it desirable to preserve the business after key persons are no longer available due to death or illness?

3. Transfer of ownership. How desirable is it that owners be able to easily dispose of their part of the business? Is it important that transfer of ownership not disrupt business functions?

4. Liability of owners. How much financial risk is each person in the business willing to take? Is it desirable to separate business and personal assets?

5. Fund raising. How much money will be needed to start up and run this business? What are likely sources of money?

6. Tax laws. Which legal form of organization minimizes the total tax load imposed on a particular business?

7. Regulation. The various legal forms of business organization are subject to varying degrees of regulation. How much time and effort does the prospective owner wish to extend on record keeping? How much information does the prospective owner wish to divulge to the public?

8. Ownership. What is the experience of the prospective owner? Is it desirable to have one or more owners? If more than one owner is favored, should ownership be equal?

9. Management. Is it desirable to have one or more managers? Should management responsibility and ownership be vested in the same person?

10. Incentives. Which legal form will provide maximum ultimate income to the owners? Will the business be able to provide motivation necessary to acquire needed managerial talents for growth and success?

B. The legal form of business organization originally chosen by owners should be reassessed periodically in light of the above factors as external conditions change. Conditions such as the following may necessitate a shift to another legal form of business organization:

1. Fund raising plans. Few businesses are financed entirely from profits. Both equity capital (i.e., money provided by owners) and traditional loan sources of funds will impose conditions on the business which protect their interests. Equity holders may, for example, like the ease of ownership transfer provided by the corporate form. Bank loan sources may prefer the partnership form backed by the personal assets of partners. Fund raising is so important in most businesses that it may change the choice of business organization when all other factors indicate that another form is preferred.

2. Obligations of owners and managers. Changes in personal lives of owners and managers may often be affected by and affect a business. Problems that originally seemed to be small may grow bigger. A change in legal form of organization may be necessitated.

3. Taxation and regulation. Taxation and regulation may begin to demand changes in the form of organization as businesses grow larger and as laws change.

4. Exploitation. Time, money, products, and people are all open to exploitation. Operating problems often convince management of a need for a different legal form of organization.

5. Growth, expansion, and sale. A change in legal form of business organization may be demanded by each of these.

Discussion Overhead for Objective 2.4

Legal Forms of Business Organization Related to Selected Decision Factors

Factor	Proprietorship	Partnership	Corporation
Formation	Least complicated. Person simply starts business activity. May need city or state license.	More complex. Partnership agreement desirable. May need city or state license.	Most complicated. State charter needed. May need city license or federal charter.
Ownership Transfer	Ownership transferred simply by sale or inheritance of business.	No formalities. But mutual agreement necessary--may be complicated.	Full or partial ownership easily transferred by sale of stock.
Business Life	Limited by life of owner or sale of business.	Limited by life and agreement of partners.	Unlimited life depending on charter and business success.
Owner Liability	Unlimited liability for owner's personal assets.	Unlimited liability for personal assets of at least one partner.	Limited to amount individual invests in stock.
Fund Raising	Limited by owner's personal assets and ability to borrow.	Limited by partners' personal assets and ability to borrow.	Fairly easy to sell stock. Borrowing based on credit capacity of corporation.
Taxation	Business income taxed as personal income of proprietor.	Business income taxed as personal income of each partner.	Business income taxed as corporate profits. Stockholders taxed individually on salary and dividend income.
Regulation	Minimum regulation. Profit not known by public.	Minimum regulation. Profit not known by public.	Subject to heavy regulation. Formal records necessary. Much financial information to stockholders and public.
Ownership	Generally sole control in owner.	By agreement or equally among partners.	By amount of stock owned by an individual.
Ownership & Management	Owner most often manager.	May have separate owners and managers.	Usually ownership and management separated.

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

QUESTIONS FOR DISCUSSION

Objective 2.4: Determine and discuss decision factors affecting the selection of an effective legal form of business organization.

A. What are some factors that should be considered before weighing pros and cons of legal forms of organization for a particular business (see Discussion Overhead for Objective 2.4)?

1) Which legal form of business organization is the most difficult to form? Which the least complicated?

2) In which legal form of business organization is ownership easily transferred? How is it transferred?

3) Which legal form of business organization most often allows limited liability to its owners? When might this form not allow its owners limited liability?

4) Which legal form of business organization allows funds to be most easily raised?

5) In which legal forms of business organization are management-owner conflicts most likely to occur?

B. What conditions might suggest reevaluation of a chosen legal form of business organization?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES

Objective 2.4: Determine and discuss decision factors affecting the selection of an effective legal form of business organization.

1. Compare the various legal forms of business organization discussed according to the following decision factors: formation, ownership transfer, business life, owner liability, fund raising, taxation, regulation, ownership, ownership and management.

2. Answer the activity handout entitled "How About You?" Are you the kind of person who would do best as a sole proprietor, as a partner, or as an employee?

UNIT 2.0

SELECTION OF EFFECTIVE LEGAL FORM OF BUSINESS ORGANIZATION

STUDENT ACTIVITIES (Con't)

Objective 2.4: Determine and discuss decision factors affecting the selection of an effective legal form of business organization.

3. Jot down answers to the following questions:

   a) Why would you want your own business?

   b) Have you worked for someone else as a manager?

   c) Have you had appropriate business training in school?

   d) Have you saved any money?

   e) If you need a partner with money or know-how that you don't have, do you know someone who would fit--someone you could get along with?

4. Ideally, which legal form of business organization would you like to have? Considering your limitations (such as money, business experience, and personality), which would you pick?

Activity Handout for Objective 2.4

How About You?

Under each question, check the answer that says what you feel or comes closest to it. Be honest with yourself.

ARE YOU A SELF-STARTER?

_____ I do things on my own. Nobody has to tell me to get along.
_____ If someone gets me started, I keep going all right.
_____ Easy does it, man. I don't put myself out until I have to.

HOW DO YOU FEEL ABOUT OTHER PEOPLE?

_____ I like people. I can get along with just about anybody.
_____ I have plenty of friends--I don't need anyone else.
_____ Most people bug me.

CAN YOU LEAD OTHERS?

_____ I can get most people to go along when I start something.
_____ I can give the orders if someone tells me what we should do.
_____ I let someone else get things moving. Then I go along if I feel like it.

CAN YOU TAKE RESPONSIBILITY?

_____ I like to take charge of things and see them through.
_____ I'll take over if I have to, but I'd rather let someone else be responsible.
_____ There's always some eager beaver around wanting to show how smart he or she is. I say let them.

HOW GOOD AN ORGANIZER ARE YOU?

_____ I like to have a plan before I start. I'm usually the one to get things lined up when the gang wants to do something.
_____ I do all right unless things get too goofed up. Then I cop out.
_____ You get all set and then something comes along and blows the whole bag. So I just take things as they come.

HOW GOOD A WORKER ARE YOU?

_____ I can keep going as long as I need to. I don't mind working hard for something I want.
_____ I'll work hard for a while, but when I've had enough, that's it, man!
_____ I can't see that hard work gets you anywhere.

CAN YOU MAKE DECISIONS?

_____ I can make up my mind in a hurry if I have to. It usually turns out OK, too.
_____ I can if I have plenty of time. If I have to make up my mind fast, I think later I should have decided the other way.
_____ I don't like to be the one who has to decide things. I'd probably blow it.

CAN PEOPLE TRUST WHAT YOU SAY?
_____ You bet they can. I don't say things I don't mean.
_____ I try to be on the level most of the time, but sometimes I just say what's easiest.
_____ What's the sweat if the other fellow doesn't know the difference?

CAN YOU STICK WITH IT?
_____ If I make up my mind to do something, I don't let anything stop me.
_____ I usually finish what I start--if it doesn't get fouled up.
_____ If it doesn't go right away, I turn off. Why beat your brains out?

HOW GOOD IS YOUR HEALTH?
_____ Man, I never run down!
_____ I have enough energy for most things I want to do.
_____ I run out of juice sooner than most of my friends seem to.

NOW COUNT THE CHECKS YOU MADE.
_____ How many checks are there beside the first answer to each question?
_____ How many checks are there beside the second answer to each question?
_____ How many checks are there beside the third answer to each question?

If most of your checks are beside the first answers, you probably have what it takes to run a business. If not, you're likely to have more trouble than you can handle by yourself. Better find a partner who is strong on points you're weak on. If many checks are beside the third answer, not even a good partner will be able to shore you up.

Source: Small Marketers Aid No. 71 (Washington, D.C.: Small Business Administration, revised August 1970).

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

OBJECTIVES

After completing this unit, the student will be able to:

Objective 3.1	Determine the assistance an accountant can provide for a small business.
Objective 3.2	Determine the assistance a lawyer can provide for a small business.
Objective 3.3	Determine the assistance a banker can provide for a small business.
Objective 3.4	Determine the assistance a management consultant can provide for a small business.
Objective 3.5	Develop other assistance information sources.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

INFORMATION SHEET

Objective 3.1: Determine the assistance an accountant can provide for a small business.

A. An accountant can help the businessperson develop an efficient accounting system; prepare financial statements and income tax returns; and, if the accountant is certified, audit the accounting records.

B. The accounting services may be performed by a local or national accounting firm, by an employee trained in accounting, by a free-lance accounting service, by professional accounting services that specialize in the entrepreneur's type of business, or by the entrepreneur.

C. The accountant is familiar with the language of business, and important decisions based on an understanding of accounting are constantly made. Expertise is needed at times generally to help in the decision-making process.

D. Larger accounting firms generally have specialists in different areas including small business.

E. When looking for an accountant or accounting firm, talk to a similar business that is successful and find out who its accountant or accounting firm is.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION

Objective 3.1: Determine the assistance an accountant can provide for a small business.

A. What are the advantages and disadvantages for hiring an accountant for a small business?

ACCOUNTANT

ADVANTAGES	DISADVANTAGES

B. What criteria (i.e., background, experiences) would you look for in an accountant for a small business?

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION (Con't)

Objective 3.1: Determine the assistance an accountant can provide for a small business.

C. What are the advantages and disadvantages for having the accounting services provided by the following: (1) local accounting firm; (2) national accounting firm; (3) business employee (both full- or part-time); (4) specialized accounting service (e.g., service stations); (5) free-lance accounting service; and, (6) small business owner?

LOCAL ACCOUNTING FIRM

ADVANTAGES	DISADVANTAGES

NATIONAL ACCOUNTING FIRM

ADVANTAGES	DISADVANTAGES

BUSINESS EMPLOYEE

ADVANTAGES	DISADVANTAGES

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION (con't)

Objective 3.1: Determine the assistance an accountant can provide for a small business.

C. (con't)

SPECIALIZED ACCOUNTING SERVICE

ADVANTAGES	DISADVANTAGES

FREE-LANCE ACCOUNTING SERVICE

ADVANTAGES	DISADVANTAGES

SMALL BUSINESS OWNER

ADVANTAGES	DISADVANTAGES

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

STUDENT ACTIVITIES

Objective 3.1: Determine the assistance an accountant can provide for a small business.

1. List the accounting services an accountant can provide to a small business. Compare your list with others in the class.

2. Contact a local accounting firm and discuss the services they could provide for a small business.

3. Visit a local small business similar to a business of interest to you and ask the owner (or manager) if the owner (or manager) uses the services of an accountant. Why did the owner choose the particular accountant, firm, or specialized accounting service?

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

INFORMATION SHEET

Objective 3.2: Determine the assistance a lawyer can provide for a small business.

A. The volume and complexities of the legal structure require the assistance of a lawyer to identify and interpret the small businessperson's rights, responsibilities, and liabilities under the law.

B. Essentially, the lawyer provides various general functions such as researching, advising, guiding, and representing. A lawyer researches the company records to determine if any past actions violated the law. One advises by explaining the legal ramifications of various courses of action. A lawyer offers guidance to help make a judgment when evaluating the various courses of action. One represents the small businessperson by communicating as a specialist, understanding the language of the law, and acting as an agent of the business.

C. Although the previous general functions are also available to large businesses, a lawyer can provide valuable assistance for specific services such as buying property, tax planning, employer-employee relations, credit problems, and other specialized areas affecting a small businessperson.

D. Generally, good business practice is to use lawyers for legal advice, not business advice.

E. Although many small businesses consider legal services only when their businesses are in trouble, consultation with a lawyer on business operations can help prevent legal problems in the future.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION

Objective 3.2: Determine the assistance a lawyer can provide for a small business.

A. Why should a lawyer be consulted regarding various business operations?

B. What are the advantages of a good relationship with a lawyer?

C. "Consult a lawyer for legal advice not business advice" -- Why is this statement important? Explain.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

STUDENT ACTIVITIES

Objective 3.2: Determine the assistance a lawyer can provide for a small business.

1. List legal services that you think a lawyer can provide a small business.

2. Contact a local law firm and list the services that the firm provides for a small business. Compare your findings with those of classmates.

3. Contact a local small business and ask the owner the legal services the business receives frequently.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

INFORMATION SHEET

Objective 3.3: Determine the assistance a banker can provide for a small business.

A. A small businessperson should have a good working relationship with a banker because the banker can provide financial services important to the success of the business.

B. The banker, who becomes involved in your business, is aware of your financial position and can provide valuable assistance concerning over-all financial matters.

C. The banker, because of his/her position in the banking community, can help provide credit information on the small businessperson's customers.

D. An important point to remember is to pick a banker, not a bank. You will be working with that individual regarding most of your financing needs. Developing confidence in one another is, therefore, important.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION

Objective 3.3: Determine the assistance a banker can provide for a small business.

A. What are the advantages of developing a good working relationship with a banker?

B. Describe the types of financial services available to a small businessman from a bank. Any non-financial services?

C. What are some of the advantages of picking a banker and not a bank?

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

STUDENT ACTIVITIES

Objective 3.3: Determine the assistance a banker can provide for a small business.

1. List all of the local banks in your area. Contact one bank and find out the services available to a small business.

2. Contact a small business and ask the owner what services were provided to him and how often does the owner use the services.

3. List the types of information a banker would need to become familiar with the small business's financial situation.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

INFORMATION SHEET

Objective 3.4: Determine the assistance a management consultant can provide for a small business.

A. A management consultant can be a generalist by being familiar with all phases of the administration of business. Or, a management consultant can be a specialist by having expertise only in certain areas.

B. A management consultant's prime objective is to detect trouble spots in a business operation and to suggest ways of overcoming them.

C. Management consultants can be costly; therefore, it is important that the problem is very clear that you want them to solve. Also, full cooperation regarding any changes must be maintained.

D. A management consultant is objective in the analysis of the business, and can rely heavily on specialized knowledge and experience.

E. In selecting a management consultant, it is always good practice to talk to businesses serviced by the consultant. Also, seek recommendations from your lawyer, accountant, or banker.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION

Objective 3.4: Determine the assistance a management consultant can provide for a small business.

A. What are some ways a management consultant can help a small business?

B. What are the advantages and disadvantages of hiring a management consultant?

MANAGEMENT CONSULTANT

ADVANTAGES	DISADVANTAGES

C. Why, as a small business owner, do you need services provided by a management consultant? Would you have confidence in the management consultant's recommendations? Why?

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

STUDENT ACTIVITIES

Objective 3.4: Determine the assistance a management consultant can provide for a small business.

1. Develop a list of management consultants or firms from your local telephone book. If available, identify their specialized services.

2. Visit a local management consultant or consulting firm and determine the types of services they provide small businesses.

3. List as many problems as you can that a management consultant can help to overcome.

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

INFORMATION SHEET

Objective 3.5: Develop other assistance information sources.

A. A trade association affiliated in the same type of business or industry as the small business can provide valuable services such as specific accounting systems, statistics for the industry, publish special publications, sponsor seminars and workshops, credit reporting, and specialized technical advice.

B. The government is a tremendous business information source for small businesses. There are many governmental agencies that provide information. Some of the agencies and some of their services are as follows:

1. Federal Reserve Banks -- Reports on business and economic conditions.
2. Internal Revenue Service -- Publishes the Tax Guide for Small Business yearly.
3. U.S. Department of Commerce -- Publishes periodic census data of population, manufacturing, and business.
4. Small Business Administration -- Provides a thorough program of management assistance which includes the following:
    a. Conferences, workshops and courses
    b. Problem clinics (small group treatment of problems under guidance of a qualified leader)
    c. Individual counseling
        1. SCORE (Service Corps of Retired Executives)
        2. ACE (Active Corps of Executives)
    d. Small Business Institute program (personal counseling from faculty, senior and graduate students of business -- limited to SBA clients)
    e. The "406 Program" (assistance to qualified individuals under Section 402 of the Equal Opportunity Act)

C. Other groups that can serve as information sources for small business are as follows:

1. Chamber of Commerce
2. Credit Bureaus
3. Better Business Bureau
4. Suppliers and equipment manufacturers
5. Educational Institutions (research bureau, libraries)

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

QUESTIONS FOR DISCUSSION

Objective 3.5: Develop other assistance information sources.

A. What are some of the services a trade association can provide a small business?

B. Describe the types of services available from the Small Business Administration, and three other governmental agencies servicing small businesses.

C. In what ways can the chamber of commerce, credit bureau, better business bureau, suppliers and equipment manufacturers, and educational institutions help small businesses?

UNIT 3.0

SELECTION OF EFFECTIVE SPECIALIZED ASSISTANCE

STUDENT ACTIVITIES

Objective 3.5: Develop other assistance information sources.

1. Prepare a list of trade associations for five types of small businesses. If available, determine what services each trade association provides.

2. Visit your local Small Business Administration office and talk to a counselor regarding the available services.

3. From the other sources of business information discussed, contact one source and identify the services, publications, etc. available to small businesses.

UNIT 4.0

FINANCING THE SMALL BUSINESS

OBJECTIVES

After completing this unit, the student will be able to:

Objective 4.1	Estimate the amount of capital required to start up and maintain business operations.
Objective 4.2	Identify and discuss sources of equity capital that might be used to start up and maintain business operations.
Objective 4.3	Identify and discuss sources of debt capital that might be used to start up and maintain business operations.
Objective 4.4	Estimate sales volume required for business operations to break even.

UNIT 4.0

FINANCING THE SMALL BUSINESS

INFORMATION SHEET

Objective 4.1: Estimate the amount of capital required to start up and maintain business operations.

A. The importance of realistically estimating the amount of capital (i.e., money, funds) required to start up and maintain a business is demonstrated by the fact that inadequate capital is one of the most common causes of small business failure.

   1. The amount of capital needed to start up and maintain business operations varies with the type of business, the legal form of business organization, the sales volume expected, the cost of equipment and labor, the kinds of products to be sold, the type of services to be provided (e.g., cash vs. credit), etc. A roadside stand offering fruit and vegetables for cash requires much less money to start and maintain, for example, than a department store which extends credit and carries a wide variety of products.

   2. Before attempting to make realistic estimates of capital required for a particular business, therefore, the prospective businessperson should consult various people who might have information regarding the amount of money other people have needed to finance similar businesses. Operating data might be obtained from the owner of a similar business. The prospective owner's banker, lawyer, and accountant would have information about money needed to enter similar businesses. The Small Business Administration and librarians would possess published information about numerous types of businesses.

B. New, and ongoing, businesses need to use capital for several purposes. Among them are the following:

   1. Initial expenses. A multitude of expenses must be met simply to start up a business. Costs may be associated with finding a suitable business location and with locating initial sources of capital. Also, provisions must be made for such things as furniture and equipment, starting inventory, decorating and remodeling, installation of equipment, utility company deposits, legal and professional fees, licenses and permits, advertising and promotion, and operating cash.

   2. Working capital. Working capital is defined as total current assets and typically consists of money invested in cash, in inventories, and in accounts receivable.

a. Cash. Although some money may be held in a small petty cash fund, cash usually consists of money deposited in a commercial bank. Since cash inflows and outflows are rarely synchronized, business must provide a cash reservoir to handle day-to-day operations.

To estimate the amount of cash required for a particular business, the relationship between expenses and sales revenue is critical (see Objective 4.4 on break-even analysis). Several factors that are unique to each business must be considered: sales volume, scale of operations, seasonality of sales, whether sales are credit or cash, credit terms given to customers, customer paying habits, and expected as well as unexpected expenses. The cash balance for a new business should be generous because of the possibility of unexpected expenses and because time may be required to generate sales and resulting cash inflows.

b. Inventories. Investment in inventories frequently represents a major part of working capital for a small business. For new businesses, determining types and quantities of products to be stocked may be difficult. Suppliers can sometimes offer advice. Also, ratios of net sales to inventory for a particular type of business published by Dun and Bradstreet or trade associations might be helpful.

Several factors need to be considered when estimating the investment required in inventories. On one hand, an owner will not have the money to stock an infinite variety of items to avoid lost sales. On the other hand, turning customers away because of out-of-stocks hurts business. Also important in determining inventory levels is the location of suppliers and the time it takes them to replenish supplies.

c. Accounts receivable. The third component of working capital consists of an investment in accounts receivable if credit sales are offered. To estimate the investment required in accounts receivable, prospective entrepreneurs must consider the following factors: the relationship between cash sales and credit sales, credit terms that are extended to customers, paying habits of credit customers, and costs associated with administering a credit program.

The prospective businessperson must realize that even though a credit sale is made, the account receivable may not turn over before inventory needs to be replenished.

Thinking only in terms of sales volume can be a disaster because as credit sales increase, the amount of working capital available to replace inventory decreases. Results can be inventory decline followed by sales decline.

d. As a general rule, the prospective entrepreneur should overestimate rather than underestimate working capital requirements. The tendency in many small businesses is to have too much money tied up in fixed assets that are hard to convert to cash. If a business must depend on daily receipts to meet daily obligations, a slump in sales or an unexpected expense could spell financial doom.

3. Fixed assets. Fixed assets are relatively permanent assets used to produce a product or to offer a service and typically include land, buildings, and equipment. The size of the fixed asset capital requirement depends to a great extent on the type of business operation. A small apparel store, for example, might lease a building and require fixed assets only in the form of furniture. In any type of business a minimum quantity of fixed assets exists to carry on operations. A one-table restaurant, for example, would be grossly inadequate in terms of fixed assets needed and would probably result in little or no profit.

Fixed asset needs should be thoroughly investigated before money is committed since dollars invested in fixed assets represent long-term commitments resulting in loss of flexibility. In general, it is desirable to minimize fixed asset investment when possible. Small new firms may decide to lease rather than to buy fixed assets because leasing arrangements reduce the amount of capital needed at the outset and provide flexibility should the business be less successful than anticipated.

To estimate the capital required for fixed assets, price quotations should be obtained from suppliers of equipment furniture, etc. The prices asked by sellers provide cost estimates for land and buildings.

4. Growth. When orders pour into a business, that growing business needs money to move to larger quarters, to add personnel, to increase inventories, etc.

C. Detailed financial estimates or projections are especially important in helping new and growing business entrepreneurs plan for, rather than fall over, financial needs.

The prospective entrepreneur should begin by writing an operating plan which describes how every facet of business (e.g., marketing, management, etc.) will be handled in the next year or two. This plan can then be translated into projected dollar needs.

To translate the operating plan into projected dollar needs, the entrepreneur should prepare a capital expenditures budget, a projected income statement, a cash flow projection, and a projected balance sheet. These projections should be made monthly during the first year of business or during times of rapid expansion. Later, quarterly or annual statements may be enough to keep management aware of needs.

1. *Capital expenditures budget*. A capital expenditures budget lists planned purchases of land, facilities, and equipment. It also lists any expected physical improvement of fixed assets.

2. *Projected income statement*. A projected income statement shows estimated operating expenses such as rent, labor, supplies, and promotion plus inventory purchases for a given period subtracted from a realistic estimate of that period's net sales. A projected income statement that showed a profit at the end of the period would indicate adequate financing and profitable operations. A loss would indicate a need for increased sales, better management control of expenses, or additional funds.

3. *Cash flow projection*. A cash flow projection is used to estimate actual cash surplus or deficit for each period. The projected income statement shows *recorded* cash and credit sales and all payments due, but the projected cash flow subtracts the *actual* bills paid from the *actual* cash collected during a given period.

4. *Projected balance sheet*. After making up a balance sheet showing what the business owns (i.e., assets), what the business owes (i.e., liabilities), and what owners have contributed (i.e., net worth) at a particular moment, the entrepreneur can work toward an ideal projected balance sheet. The capital expenditures budget, income estimated on the projected income statement, and estimated cash from the projected cash flow statement are used to make the projected balance sheet.

Discussion Overhead for Objective 4.1

Projected Income Statement
Fun Fashions
Year 1

Net Sales		$150,000
Cost of Goods Sold		80,000
Gross Profit		$ 70,000
Operating Expenses:		
Depreciation	$ 7,000	
Payroll	16,000	
Payroll Taxes & Fringe Benefits	2,000	
Management Salary	20,000	
Supplies	500	
Miscellaneous Contract Expense (Cleaning, Trash, Extermination, Equipment Rental)	1,000	
Advertising & Promotion	4,000	
Utilities	2,000	
Telephone	400	
Legal & Accounting Fees	1,000	
Repair & Maintenance	2,000	
Taxes, Licenses, & Fees	2,000	
Insurance	2,000	
Postage & Freight	1,000	
Dues & Subscriptions	100	
Total Expenses		$ 61,000
Net Profit Before Taxes		$ 9,000
Federal Income Taxes (Corporation only)		2,000
Net Profit		$ 7,000*

*Note: Net Profit transfers to Projected Balance Sheet

Discussion Overhead for Objective 4.1

Projected Cash Flow Statement
Fun Fashions
Year 1

	J	F	M	A	M	J	J	A	S	O	N	D
Cash in Bank (Start of Month)	$	$	$	$	$	$	$	$	$	$	$	$
Petty Cash (Start of Month)												
Total Cash												
Expected Cash Sales												
Expected Collections												
Other Money Expected												
Total Receipts												
Total Cash & Receipts												
All Disbursements (for month)												
Cash Balance at End of Month	$	$	$	$	$	$	$	$	$	$	$	*$17,000

*Note: Cash Balance (End of Year) transfers to Projected Balance Sheet for End of Year.

Adapted from: "Business Plan for Retailers" (Washington, D.C.: Small Business Administration), Small Marketers Aid No. 150.

Discussion Overhead for Objective 4.1

Projected Balance Sheet
Fun Fashions
For End of Year 1

Assets			
Current Assets:			
Cash	$17,000		
Accounts Receivable	15,000		
Inventory & Supplies	21,000		
Total Current Assets		$53,000	
Fixed Assets:			
Buildings	72,000		
Equipment	18,000		
Total Fixed Assets		90,000	
Total Assets			$143,000
Liabilities & Owners' Equity			
Current Liabilities:			
Accounts Payable	$ 1,000		
Note Payable to Bank	4,000		
Taxes Payable	9,000		
Total Current Liabilities		$14,000	
Long Term Liabilities			
Loan Payable to SBA		50,000	
Total Liabilities			$ 64,000
Owners' Equity:			
Common Stock		72,000	
Retained Earnings		7,000	
Total Owners' Equity			79,000
Total Liabilities & Owners' Equity			$143,000

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION

Objective 4.1: Estimate the amount of capital required to start up and maintain business operations.

A. What are factors causing differences in the amount of capital needed to start up and maintain specific business operations?

B. Who might prospective entrepreneurs contact to help make estimates of capital required for their particular businesses more realistic?

C. For what purposes is capital typically used in new and ongoing businesses?

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION (Con't)

Objective 4.1: Estimate the amount of capital required to start up and maintain business operations.

D. Define the following, and give examples of each:

(1) Initial expenses.

(2) Working capital.

(3) Fixed assets.

E. What factors should be considered when prospective entrepreneurs estimate capital required to finance the following:

(1) Cash?

(2) Inventory?

(3) Accounts Receivable?

(4) Fixed Assets?

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION (Con't)

Objective 4.1: Estimate the amount of capital required to start up and maintain business operations.

F. Net sales of a particular type of small business is typically 5 times inventory, and net sales for a specific business are estimated at $500,000. How much inventory capital is the specific business likely to require?

G. What information is shown on the following (see Discussion Overheads for Objective 4.1):

(1) Capital Expenditures Budgets?

(2) Projected Income Statements?

(3) Projected Cash Flow Statements?

(4) Projected Balance Sheets?

UNIT 4.0

FINANCING THE SMALL BUSINESS

STUDENT ACTIVITIES

Objective 4.1: Estimate the amount of capital required to start up and maintain business operations.

1. Assume that you are thinking about opening a hardware store.

   You estimate that your annual net sales will be about $100,000.

   To help estimate expenses, you checked with your trade association and read Ratio Analysis for Small Business listings. You found that in your line of business cost of goods sold is typically 66.05 percent of sales, owner-manager salary is typically 7.15 percent of sales, etc.

   You have started to prepare a projected income statement (see Student Activity Handout for Objective 4.1) using ratios to estimate expenses.

   What is your estimated net profit for Year 1?

2. Answer the following:

   (a) Where would your projected net income after taxes appear if you were to prepare a projected balance sheet?

   (b) In what section of a projected balance sheet would your capital expenditures budget appear?

   (c) Where on a projected balance sheet would your projected cash flow appear?

Student Activity Handout for Objective 4.1

Projected Income Statement
Store Name ____________
Year 1

	Percent of Sales		Projection	
Net Sales		100.00		$100,000
Cost of Goods Sold		66.05		66,050
Gross Profit		33.95		$ 33,950
Operating Expenses:				
Salary Expense	16.75		$	
Postage & Office Supplies	.40			
Advertising & Promotion	1.55			
Donations	.05			
Telephone	.30			
Accts. Receivable Losses	.15			
Delivery Expense	.50			
Depreciation	.60			
Rent	2.70			
Repairs	.10			
Utilities	.80			
Insurance	.80			
Taxes (Excluding Fed. Income)	1.10			
Interest on Loans	.05			
Miscellaneous Expense	1.20			
Total Expenses		27.05		$
Net Profit Before Taxes		6.90		$

Adapted from: "Business Plan for Retailers" (Washington, D.C.: Small Business Administration), Small Marketers Aid No. 150.

UNIT 4.0

FINANCING THE SMALL BUSINESS

INFORMATION SHEET

Objective 4.2: Identify and discuss sources of equity capital that might be used to start up and maintain business operations.

A. Equity capital is ownership money which is not repaid but which instead entitles the investor to a voice in business operations and a percentage of future profits. Since equity represents ownership, it appears on the balance sheet as net worth or owners' equity.

Some degree of risk is associated with all sources of capital. Because existing owners jeopardize management control with equity financing, equity capital is said to involve a very high degree of risk.

Most of the capital required to start up a business is obtained from equity sources. Equity financing is called for when organizers cannot provide a minimum of 50 to 60 percent of the total capital required by a small business.

B. Sources of equity capital are partially determined by the selected form of business organization. Potential sources of equity money include the following:

1. Sole proprietorship. When one person finances a business using only his or her cash, the business is called a sole proprietorship. Most small entrepreneurs start their own businesses by using their own money. Equity sources in a sole proprietorship are limited to personal savings, securities or real estate personally owned, or other personal property of high value.

2. Partnership. When two or more persons go into business as co-owners, a partnership is formed. Equity sources in a partnership are much the same as those in the sole proprietorship. Equity can be added to a business, in this situation, with (i.e., general partnership) or without (i.e., limited partnership) sharing business responsibilities and liabilities. Often a person with good ideas and experience but inadequate funds will team up with another person who can provide the needed capital for the business.

3. Corporation. When three or more individuals apply to and are accepted by a particular state for a corporate charter, a corporation is formed. Ownership is represented by the number of shares of stock each person holds. The corporation is

considered the most efficient type of legal business organization for obtaining equity capital since, except where special agreements exist, each person's liability for the obligations of the business is limited by the amount of his or her investment in stock.

Sources of equity capital for a corporation involve simply sale of stock. To obtain capital, two classes of stock are commonly sold: common and preferred. Common stock provides maximum potential return in good times to stockholders since dividends (i.e., payments to stockholders) vary with profits. Should the business fail, however, common stockholders are repaid after all creditors and all other owners. Preferred stockholders have a priority position in cash of business failure since they must be paid in full before common stockholders. Preferred stock offers a smaller potential return to stockholders in good times, however, since dividends are fixed and guaranteed and do not vary with earnings.

4. Nonprofessional investors. Before asking professional investors for funds needed, the prospective small entrepreneur should contact anyone who might contribute to his or her business out of goodwill and faith. Nonprofessional sources of funds might include parents, rich relatives, friends, or co-workers. Also, bankers and accountants can often help find wealthy individuals who are looking for investment opportunities as a tax shelter.

5. Venture capital groups. Groups of investors frequently form "venture capital" associations to provide equity capital to promising small businesses. These groups typically prefer to buy stock in corporate organizations and usually favor certain locations and industries. Such equity money is not easily obtained because these groups do not make charitable contributions. Rather, they are in business to gamble that a firm will return their investment--many times over. Venture capitalists search for companies that will grow and analyze business plans focusing on management capability, product superiority, and growth industries.

6. Small Business Investment Companies (SBICs) and Minority Enterprise Small Business Investment Companies (MESBICs). Private venture capital groups have traditionally not been able to supply capital needs of small business in general and of minority-owned small business in particular. As a result, the federal government authorized Small Business Investment Companies and Minority Enterprise Small Business Investment Companies. SBICs and MESBICs are privately owned venture capital firms eligible for federal loans to boost spending money they allocate to small business and small businesses owned by minority and socially or economically deprived groups respectively.

   Like privately funded venture capital groups, SBICs and MESBICs prefer to buy stock in corporate organizations and usually favor specific locations and industries. Each SBIC and MESBIC company is listed with its preferences in The Directory of Operating Small Business Investment Companies published by the Small Business Administration. SBICs and MESBICs are also looking for a healthy return on their investment. As a result, they tend to focus on management capability, product vitality, healthy industries, and established vs. beginning businesses.

7. State Business and Industrial Development Corporations (SBIDCs). Frequently State Business and Industrial Development Corporations are created to further statewide prosperity and employment by helping small businesses with equity and debt financing. Oil companies, utility companies, and large retail chains are usually owners in development corporations which provide equity money in states where SBIDCs make funds available. Details are handled through banks, savings and loan companies, and insurance companies which are SBIDC members.

8. Reinvested profits. Retained profits (i.e., earnings plowed back into the firm) are a major source of equity funds for financing expansion of small, established businesses. While reliance on retained earnings, sometimes labeled "internally generated funds," may limit growth; it is a conservative approach to financing in that no risk is involved regarding loss of management control of the firm.

Discussion Overhead for Objectives 4.2 and 4.3

Selected Sources of Capital

Type of Money	Source
Equity	Sole Proprietorship Partnership Corporation Nonprofessional investors Venture capital groups SBICs MESBICs SBIDCs Retained profits
Debt	Commercial banks SBA Life insurance companies Savings and loan associations Leasing companies Commercial finance companies Inventory and equipment suppliers Personal finance companies

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION

Objective 4.2: Identify and discuss sources of equity capital that might be used to start up and maintain business operations.

A. What is equity capital? How and where does it appear on the entrepreneur's balance sheet?

B. What is the risk associated with equity capital?

C. What are potential sources of funds for small business owners who choose to use equity financing (see Discussion Overhead for Objectives 4.2 and 4.3)? Discuss each briefly.

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION (Con't)

Objective 4.2: Identify and discuss sources of equity capital that might be used to start up and maintain business operations.

D. Compare and contrast venture capital groups and Small Business Investment Companies as sources of equity funds. Which of these two sources would you most likely use? Why?

E. What are advantages and disadvantages of common vs. preferred stock to the investor? To the corporation?

UNIT 4.0

FINANCING THE SMALL BUSINESS

STUDENT ACTIVITIES

Objective 4.2: Identify and discuss sources of equity capital that might be used to start up and maintain business operations.

1. Contact your local Small Business Administration office and ask what equity funds are available. How does an entrepreneur qualify for such funds?

2. Visit a successful small business in your community. Ask the owner general details about how he or she financed start-up operations. What sources of funds are used now for maintaining operations?

3. List and briefly describe sources of equity funds available to the small business entrepreneur.

UNIT 4.0

FINANCING THE SMALL BUSINESS

INFORMATION SHEET

Objective 4.3: Identify and discuss sources of debt capital that might be used to start up and maintain business operations.

A. Debt capital is borrowed money which must be repaid with interest but which usually does not give the lender any ownership control. Since debt capital represents loans requiring repayment, it appears on the balance sheet under liabilities. Borrowed capital and associated interest are usually repaid out of profits and/or sale of assets.

The risk involved with debt capital, although deemed less than the risk associated with equity money, is that the trust of creditors in owners usually must be backed (i.e., secured) by something of value such as assets. If the borrower fails to repay the debt, the creditor normally claims the tangible security put up by the owner. Although debt sources accept security for business loans, this backing is usually considered secondarily. Loan approval generally rests primarily on the business owner's ability to repay as indicated by business profitability, management expertise, and the owner's credit rating.

Usually organizers of new businesses seek capital from debt sources after they are able to provide at least 50 percent of the capital they need through equity funds. Even though lenders tend to be more numerous than equity investors, borrowed money can be as difficult as equity money to obtain.

B. Sources of debt capital can be grouped in terms of risk and in terms of institutions. Most entrepreneurs turn to banks and to the Small Business Administration when debt financing since less risk is associated with these institutions. Potential sources of debt capital include the following:

1. Commercial banks. Commercial banks are one of the most economical sources of debt capital available to a small business and provide more debt to small businesses than any other source--either directly or indirectly through finance companies and trade suppliers which borrow from banks. Since management decisions as well as government regulations influence loan policies and since banks are a major source of debt capital for small businesses, it behooves the small business owner to develop and maintain a good relationship with a commercial banker.

Banks provide numerous types of financing including the following:

a. Commercial loans. Commercial loans are for short-term (i.e., less than 1 year) needs, require repayment in a lump sum in three to six months, and may or may not require security. If the loan exceeds a specified amount, the bank may require that the borrower maintain a "compensating balance" (i.e., a reserve of cash in a bank account).

b. Term loans. Term loan arrangements usually provide funds for up to five years, spell out conditions to which the business must adhere, and may or may not require security. The principal (i.e., amount of money borrowed) and interest is repaid by periodic installments.

c. Bank credit cards. An entrepreneur can offer credit to customers without financing accounts receivable or assuming any credit risk by accepting bank credit cards such as Visa and Master Charge. The cost to the entrepreneur is usually 5 or 6 percent of a credit sale.

d. Equipment financing and leasing. Often commercial banks make loans on equipment, and the equipment is used as security. They also can arrange for equipment to be leased.

e. Real estate loans. Banks offer real estate loans to finance purchase, construction, or improvement of buildings and to acquire land. Such loans are always secured by the asset financed.

f. Accounts receivable financing. Banks will generally extend a revolving line of credit (i.e., funds are continually advanced, repaid, and readvanced) on accounts receivable pledged as security. If the accounts are bad, they must be replaced with good ones. The entrepreneur, therefore, is left with collection costs and problems.

g. Factoring. Many banks contain factoring departments which buy accounts receivable. This arrangement eliminates the cost of credit and collections in the small business. Sales may be cut back under this arrangement, however, if certain customers are deemed unacceptable credit risks by the bank.

h. Inventory financing. Banks frequently offer a revolving line of credit on inventories pledged as security. The entrepreneur pays off the inventory loan as accounts receivable are collected.

2. Small Business Administration. The Small Business Administration was established in 1953 by the federal government to administer funds appropriated by Congress to assist small businesses in need of intermediate- and long-term funds. Interest rates on

SBA loans, because the SBA is committed to public service, are usually lower than those on bank loans.

Since SBA caters to businesses that have difficulty obtaining bank loans without its guarantee, its clients are usually somewhat risky businesses and may be undercapitalized, may lack sufficient security, or may have an imperfect track record. To offset these risks, the SBA sets ceilings on loans and offers management assistance to businesses.

SBA loans are of various types and may be "direct" loans or loans supplied in "participation" with commercial banks. Direct loans of up to $100,000 can be provided if adequate security is available. In the bank participation arrangement, the SBA supplies up to 75 percent of the loan needed or a maximum of $150,000, while the bank supplies the remaining 25 percent.

3. Life insurance companies. Life insurance companies often provide debt capital to low-risk, established businesses on a secured basis. These companies also provide long-term, low-interest loans to policyholders based on the cash value of the individual's policy.

4. Savings and loan associations. Savings and loan associations provide small businesses with two sources of debt capital. The small entrepreneur may obtain funds by mortgaging the family home. Also, all associations make real estate improvement loans.

5. Leasing companies. Leasing companies lease buildings and equipment to businesses at fixed rental rates for specific time periods. The advantage to rentals is that they reduce capital requirements initially.

6. Inventory and equipment suppliers. Because the success of customers contributes to their own success, trade suppliers often permit small businesses to buy inventory on credit (i.e., usually for 30, 60, or 90 days) and equipment on an installment basis (i.e., usually financed for up to 5 years with a 20 or 30 percent down payment requested).

7. Commercial finance companies. Commercial finance companies provide small businesses with funds for a variety of purposes under a variety of arrangements. They often extend, for example, secured and unsecured loans for inventory, accounts receivable, and equipment.

8. Personal finance companies. Personal finance companies loan comparatively small amounts of money for short term on a secured basis. They take risks and accept security that other financial institutions would deem unacceptable. Because of the high cost associated with such loans, personal finance companies should be considered as a last resort.

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION

Objective 4.3: Identify and discuss sources of debt capital that might be used to start up and maintain business operations.

A. What is debt capital? How and where does it appear on the entrepreneur's balance sheet?

B. How would trade credit be listed on an entrepreneur's balance sheet? How would it be listed on a supplier's balance sheet?

C. Compare the risk associated with debt capital to that associated with equity capital. Considering only risk, which would you prefer to use? What other factors can you think of that might influence your decision to use debt vs. equity capital?

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION (Con't)

Objective 4.3: Identify and discuss sources of debt capital that might be used to start up and maintain business operations.

D. What are potential sources of funds for small business owners who choose to use debt financing (see Discussion Overhead for Objectives 4.2 and 4.3)? Discuss each briefly.

E. Why should personal finance companies be considered a last resort for obtaining debt capital?

F. What are the two sources of debt capital most often used by small business entrepreneurs? Why is this so?

UNIT 4.0

FINANCING THE SMALL BUSINESS

STUDENT ACTIVITIES

Objective 4.3: Identify and discuss sources of debt capital that might be used to start up and maintain business operations.

1. Contact your local Small Business Administration office and ask what types of loans are available. How does an entrepreneur qualify for such financing?

2. Visit a local commercial bank branch. Ask what types of loans are available to small businesses and what each requires of the entrepreneur.

3. List and briefly describe sources of debt capital available to the small business entrepreneur.

UNIT 4.0

FINANCING THE SMALL BUSINESS

INFORMATION SHEET

Objective 4.4: Estimate sales volume required for business operations to break even.

A. Break-even analysis, a supplement to estimating capital needs, is a management planning and control device for understanding the relationship between fixed and variable costs and sales revenue at different levels of operation. With this technique information in financial statements is used to estimate how much must be sold under given conditions for business to break even in the future (i.e., to just cover costs with no profit and no loss).

An accurate break-even chart is useful for several reasons. It reveals the probable level of output required to cover the expense of being in business. It provides an estimate of the effect on profits resulting from expansion or contraction of sales volume. It also helps management to analyze the prospects of decreasing variable costs, decreasing fixed costs, increasing sales price, and increasing the number of units sold to increase profits.

Some caution should be exercised in using break-even analysis. The entrepreneur must realize that the break-even point is an estimate that is not "etched in stone" since the chart is based on certain assumptions. The analysis assumes, for example, that variable costs increase at a constant rate, that fixed costs remain the same over a range of production, and that no changes in the market will affect selling price. If costs increase or decrease or if sales price has to be raised or lowered, the break-even point will change.

B. Since firms break even where sales revenue equals total costs, the entrepreneur must think in terms of sales revenue, fixed expenses, and variable expenses when using break-even analysis.

1. Sales revenue. Sales revenue is equal to the number of units sold (i.e., volume) times the sales price per unit.

2. Fixed expenses. Fixed expenses are those which do not change with changes in sales volume. Fixed expenses stay the same regardless of sales. Set monthly rent paid for store premises is a good example of a fixed expense since rent is the same each month and must be paid whether sales are good or bad. Typically, fixed expenses for a small firm include rent expense, skeleton-staff salaries, property taxes, and insurance expense.

3. Variable expenses. Variable expenses are those which change as the sales volume of a business changes. Utility expenses billed on a usage basis are a good example of variable expense since they have a tendency to rise with increased sales volume. Typical variable expenses include cost of goods sold, utility (e.g., telephone, electricity, water, and gas) expenses, advertising and promotion expense, and sales and office staff salary expense.

C. The break-even point may be determined by using a formula or by using a chart.

1. Break-even chart. A break-even chart can be easily constructed once revenue and expense estimates are made (see Discussion Overhead for Objective 4.4).

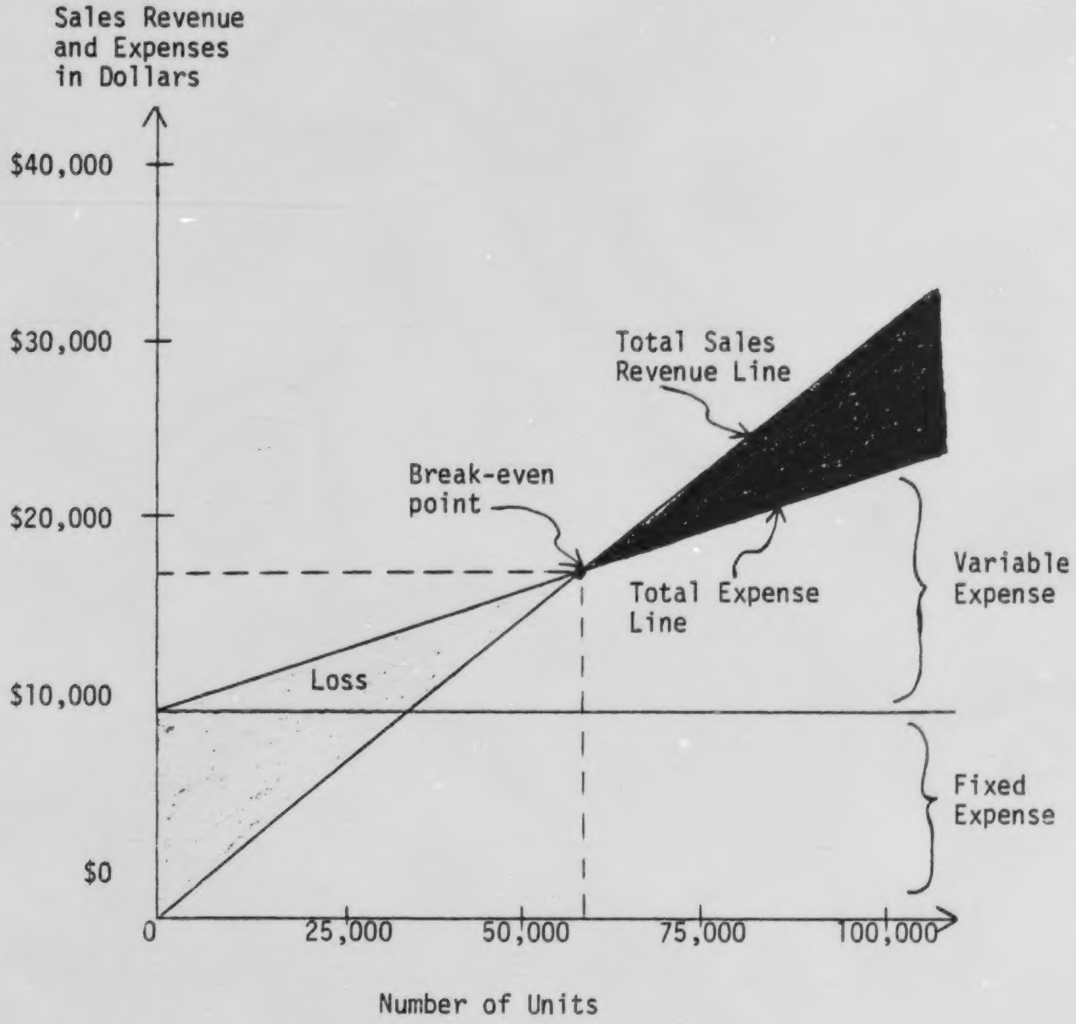
   The vertical axis represents dollars of cost and sales, and the horizontal axis represents sales volume of operation in units. Fixed expenses are portrayed as a horizontal section since they do not change with changes in volume. Variable expenses are represented by an upward slanting section because they vary with output. Combined fixed and variable expenses (i.e., total expenses) are represented by the area under the total expense line. The area between the sales line and the total expense line reveals profit or loss of a business at various levels of volume. Because sales just cover total expenses at the intersection of the sales revenue line and the total expense line, the intersection is called the break-even point.

2. Break-even formula. Use of a formula to figure a firm's break-even point gives a more precise estimate than does use of the break-even chart. One break-even formula is as follows:

$$\text{BE Point in Sales Dollars} = \frac{\text{Total Fixed Costs}}{1 - \dfrac{\text{Total Variable Costs}}{\text{Corresponding Sales Volume}}}$$

Discussion Overhead for Objective 4.4

Break-even Chart



UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION

Objective 4.4: Estimate sales volume required for business operations to break even.

A. What is break-even analysis? What are its uses?

B. Would you "get the ranch" on your calculated break-even point? Why or why not?

C. To use break-even analysis, the entrepreneur must think in terms of sales revenue, fixed expenses, and variable expenses. Briefly, what are each of these?

UNIT 4.0

FINANCING THE SMALL BUSINESS

QUESTIONS FOR DISCUSSION (Con't)

Objective 4.4: Estimate sales volume required for business operations to break even.

D. What things are portrayed on a break-even chart (see Discussion Overhead for Objective 4.4)?

E. Suppose you plan to open a store. You estimate your fixed expenses for the first year at about $9,000. You believe your variable expenses will be about $700 for every $1,000 of sales. Using the break-even formula, what is your estimated break-even point in sales dollars?

UNIT 4.0

FINANCING THE SMALL BUSINESS

STUDENT ACTIVITIES

Objective 4.4: Estimate sales volume required for business operations to break even.

1. Using the information and directions given below, prepare a break-even chart (see Student Activity Handout for Objective 4.4):

   (a) Assume that you are seriously thinking about leasing space in a shopping center to open a gift shop. You want to know how many gifts you must sell on the average per day before you begin to make a profit.

   You and your accountant estimate that variable costs will be about $.40 for every $1.00 of sales and that fixed costs will be about $9,000 a month. The average gift in your store will sell for about $2.50.

   (b) On the handout given you, construct a break-even chart.

   (1) Draw a straight line parallel to the horizontal axis to show fixed costs which would be the same regardless of the number of gifts you sold.

   (2) Draw a second line beginning at the fixed cost point on the vertical axis and increasing at the rate of $.40 per $1.00 of sales. This line shows total costs.

   (3) Draw a straight line beginning at zero and increasing at the rate of $2.50 per average gift to show total sales revenue.

   (4) Draw a dot where the total cost and total sales revenue lines intersect--labeling it "break-even point." Shade and label profit and loss areas.

   (5) Draw dotted lines from the break-even point down to the horizontal axis and across to the vertical axis.

UNIT 4.0

FINANCING THE SMALL BUSINESS

STUDENT ACTIVITIES (Con't)

Objective 4.4: Estimate sales volume required for business operations to break even.

2. Use the break-even chart you just constructed to answer the following questions:

   (a) Your gift store would begin to make a profit when it brought in how much monthly sales revenue? Or sold how many gifts per month?

   (b) Your gift store would begin to make a profit when it sold about how many gifts per day?

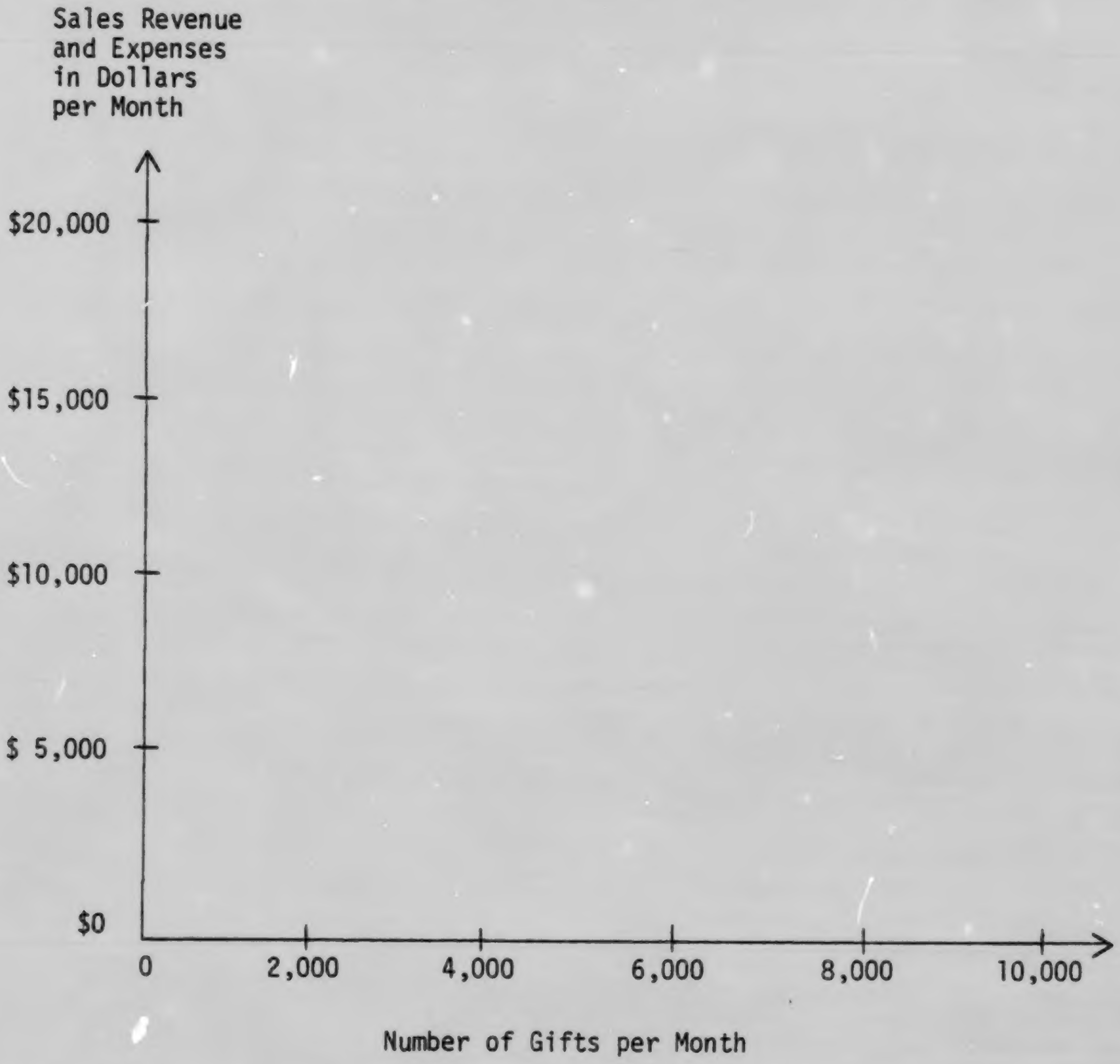
   (c) Assume you could maintain current variable costs and sales prices while reducing your fixed costs by closing the store on Sunday afternoons. Would you need to sell more or fewer gifts per month to break even?

   (d) Assume you could maintain current fixed costs and sales prices. If your variable costs were to increase for some reason, would you need to sell more or fewer gifts per month to break even?

   (e) Assume you could increase sales while maintaining current fixed costs and variable costs. In which direction would your break-even point move?

Student Activity Handout for Objective 4.4

Break-even Chart



UNIT 5.0

SELECTING A LOCATION

OBJECTIVES

After completing this unit, the student will be able to:

Objective 5.1	Determine factors to consider in selecting a town, city or geographic area for a business.
Objective 5.2	Determine factors to consider in choosing a particular area of the town or city for a business.
Objective 5.3	Identify a specific site to locate a business.

UNIT 5.0

SELECTING A LOCATION

INFORMATION SHEET

Objective 5.1: Determine factors to consider in selecting a town, city or geographic area for a business.

The factors to consider in choosing a particular location vary as to a retailing, wholesaling, or service business. Generally these factors are determined by the type of good or service to be sold and the particular market one wishes to serve.

For instance, a manufacturing concern must consider proximity to suppliers and customers, available transportation, labor and power costs, state and local taxes and regulations.

A retail store owner's primary concerns will be local traffic patterns, parking availability, neighboring businesses and institutions. All prospective owners should outline their needs -- present and future -- and then locate a unit that suits their requirements.

The choice of an area to locate is usually influenced by personal factors, economic characteristics, population trends and purchasing power, and competition factors.

A. Personal factors -- Time and money usually limit the amount of research needed to survey various geographic areas other than "your own background." Personal questions that need to be asked are:

   1. Should I locate near, or away from, friends and relatives?

   2. Do I have the available funds and time to properly research other areas?

   3. Do I desire to live in a particular location (particular part of the country)?

   4. Should I take advantage of established business connections in a location?

   5. Do I have a need to supervise other personal or business interests in the area?

B. Economic characteristics -- It is extremely important to know the trading area in the area of which you will serve. To identify this trading area you need to know:

   1. Population trends

   2. Distribution of purchasing power

   3. Size of the competition

Preference should be given to a growing town or city, one in which the income of its people is steady and regular.

C. Population trends and purchasing power -- The demographics of a particular area are very important in determining ones location after the trading area has been established. The following factors should be analyzed:

1. Population -- males, females, families
2. Trend in population -- increasing? decreasing?
3. Income -- purchasing power
4. Age
5. Type of occupations
6. Homeowners
7. Means of transportation
8. Leisure activities

Statistics may be obtained from the Bureau of Labor Statistics of the U.S. Department of Labor and local sources of information such as Inside Phoenix.

D. Competition -- The U.S. Census Bureau provides information on specific data concerning retail, wholesale, and service businesses. Such data includes:

1. The number of stores by state and county
2. The amount of sales volume
3. The number of employees

Various questions to consider will be:

1. The number of stores there that handle my lines of merchandise is __________________?
2. How many of these stores look prosperous?
3. How many look as though they are barely getting by?
4. How many similar stores went out of business in this area last year?
5. How many new stores opened up in the last year?
6. What price line does competition carry?
7. Which store or stores in the area will be your biggest competition?

UNIT 5.0

SELECTING A LOCATION

QUESTIONS FOR DISCUSSION

Objective 5.1: Determine factors to consider in selecting a town, city or geographic area for a business.

A. How can the size of a trading area be estimated?

B. Discuss each of the following statements:

(1) It is sound judgment to locate away from your competition.

(2) An area with sporadic income patterns and high unemployment would be a poor location for any business.

(3) Good service is the prime customer or clientele consideration, not store location.

C. What are the advantages and disadvantages in locating a retail or service business in a small town?

SMALL TOWN

ADVANTAGES	DISADVANTAGES

UNIT 5.0

SELECTING A LOCATION

STUDENT ACTIVITIES

Objective 5.1: Determine factors to consider in selecting a town, city or geographic area for a business.

Using the type of business you have selected, determine the following:

1. Identify the town, city or geographic area you plan to locate in. Discuss your personal reasons for locating here.

2. Collect various information on the economic characteristics and the population trends and purchasing power of this area. (Obtain from the Chamber of Commerce).

3. List information on what you consider your major competition to be.

UNIT 5.0

SELECTING A LOCATION

INFORMATION SHEET

Objective 5.2: Determine factors to consider in choosing a particular area of the town or city for a business.

A. Once the community in which you plan to locate has been established, the next consideration should be the general location within that community. Different types of business consider a variety of reasons for general location. Retailer service firms consider accessibility to their customer while wholesalers are concerned with warehouse space, delivery routes and retailers within the local market. A manufacturing business must consider its nearness to suppliers, state and local taxes and regulations, transportation costs and services, labor supply, market trends, and costs of utilities.

B. Retail and Service Location -- Retail area selection depends on the type of shopping district the entrepreneur is interested in. These include:

1. Central Shopping or Downtown District -- Factors to consider: parking, ease of public transportation, rental costs
2. Major Traffic Routes -- Factors to consider: amount of passing traffic, kind of traffic, traffic speed
3. Suburban Shopping Districts -- Include neighborhood shopping center, community shopping center and regional shopping center -- Factors to consider: Size of the community it serves, distance people have to travel to reach the shopping area

C. Because of the nature of the various shopping areas a retailer also must consider the following:

1. Amount of rent required
2. Clientele
3. Nature of product
4. Expected volume of business
5. Restrictive ordinances
6. History of the site

D. Wholesaler's Location -- Wholesalers have many of the same needs and desires of retailers with some special considerations. They desire:

1. To know the local market -- amount of retailers within a certain area (usually 10-15 miles).
2. A town with stability of income
3. A diversified industry
4. A lack of competition from other wholesalers

E. Manufacturer's Location -- The manufacturer is generally more interested in the future conditions than immediate advantages because of the costs of re-locating.

UNIT 5.0

SELECTING A LOCATION

QUESTIONS FOR DISCUSSION

Objective 5.2: Determine factors to consider in choosing a particular area of the town or city for a business.

A. What types of stores benefit most from locating near their competition?

B. What market do downtown stores and service businesses serve? Why?

C. Why are long-range factors more important to a new manufacturer than to a retailer or service business?

UNIT 5.0

SELECTING A LOCATION

STUDENT ACTIVITIES

Objective 5.2: Determine factors to consider in choosing a particular area of the town or city for a business.

Using the type of business you selected for Objective 5.1, identify the factors of information you would consider in choosing a particular area of the town, city, or geographic area. Be specific!

UNIT 5.0

SELECTING A LOCATION

INFORMATION SHEET

Objective 5.3: Identify a specific site to locate a business.

After the general location of a business has been decided, the next decision will be the specific site. Retail and service businesses have similar site considerations. Wholesalers and manufacturers have various specific needs as to site location.

A. Retail and Service -- Studies have indicated that a poor location has led to many retail and service establishment failures. Therefore, the specific building site is a determining factor in success. The following factors need to be considered:

   1. Accessibility of the business to customers (customer traffic)
   2. Amount of rent and terms of the lease
   3. Traffic volume and patterns
   4. Competition
   5. Parking availability
   6. History of the site

B. Wholesalers -- In many towns and cities specific areas are set aside for wholesalers. The major consideration for a wholesaler is the location of the local market they will serve. Other considerations include:

   1. Cost of warehouse space
   2. Amount of warehouse space
   3. Accessibility to the type of transportation needed to move your products

C. Manufacturers -- Generally the manufacturer will locate within the corporate limits of the community. The factors to consider are:

   1. Cost and accessibility of land
   2. Taxes
   3. Waste disposal

4. Building zones -- future expansion area
5. Shipping facilities and transportation access
6. Utilities

UNIT 5.0

SELECTING A LOCATION

QUESTIONS FOR DISCUSSION

Objective 5.3: Identify a specific site to locate a business.

A. Why would a retail or service business consider different factors to locate than a wholesaler or manufacturer?

B. What is meant by the accessibility of a business firm?

UNIT 5.0

SELECTING A LOCATION

QUESTIONS FOR DISCUSSION (Con't)

Objective 5.3: Identify a specific site to locate a business.

C. In what cases would it be desirable to locate near your competition as a:

(1) Retailer?

(2) Service Business?

(3) Wholesaler?

(4) Manufacturer?

UNIT 5.0

SELECTING A LOCATION

STUDENT ACTIVITIES

Objective 5.3: Identify a specific site to locate a business.

1. Using the type of business you have selected, determine specific information about a particular site in terms of those factors you need to consider as a retailer, service business, wholesaler or manufacturer.

2. Combine the information you gathered in the student activities for Objectives 5.1 and 5.2. Add to this the following:

   (a) Address of your business.

   (b) General description of the neighborhood in which you are locating.

   (c) List of competitors.

   (d) Other areas you considered and why you did not choose those areas.

   (e) Why this site location is the best for your business.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

OBJECTIVES

After completing this unit, the student will be able to:

Objective 6.1	Determine the necessary information in evaluating a building (physical facility) for a business.
Objective 6.2	Identify the equipment needs for a business.
Objective 6.3	Determine the most effective physical layout for a business.
Objective 6.4	Describe the necessary criteria needed to create an effective business image through the physical appearance of the building and layout.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

INFORMATION SHEET

Objective 6.1: Determine the necessary information in evaluating a building (physical facility) for a business.

After the specific store site has been chosen, it is necessary to secure a building. Often an existing building is one of the reasons for specific site location. The building should be able to be adapted to the particular activities of the business involved. The major considerations are:

A. The nature or function of the business

B. Physical condition, construction

C. Exterior appearance

D. Lighting, plumbing, color, heating/air conditioning

A. When considering a building, the activities of the business must be considered. The building must be able to be physically set up for your particular business.

Retail stores need to be concerned with selling space and sales-supporting space as well as customer accessibility. Service businesses require ease of customer accessibility as well as possible delivery needs. Manufacturers must be able to receive raw materials and wholesalers definitely need to consider storage space.

B. Safety of customers and employees is the number one concern when considering the building. Contruction materials as well as the construction itself should be investigated.

Possible future expansion should be considered. Can the building be adapted for other uses? In five or ten years, will we have to move?

C. Company image is often times dictated initially by the mere appearance of the business building. The front of the building, especially in retail business, is a prime sales promotion device.

D. Heating/air conditioning, lighting, and plumbing should all be checked and maintained. Lighting should not only be functional but decorative as well. Color is of utmost importance in a retail store. Manufacturers also use color to create an interesting atmosphere for routine jobs.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION

Objective 6.1: Determine the necessary information in evaluating a building (physical facility) for a business.

A. As a manufacturer or wholesaler, should as much emphasis be placed on the building front as a retail store front?

B. What factors must be considered while evaluating a building for a:

(1) Retail Business?

(2) Service Business?

(3) Wholesale Business?

(4) Manufacturing Business?

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION (Con't)

Objective 6.1: Determine the necessary information in evaluating a building (physical facility) for a business.

C. Discuss the building in terms of your products and services while considering the function of your business, appearance, and layout space.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

STUDENT ACTIVITIES

Objective 6.1: Determine the necessary information in evaluating a building (physical facility) for a business.

1. For your business, list the factors you would consider in evaluating your building.

2. Draw a sketch of your building. Include a supplementary sketch showing the front of the building.

3. Estimate the cost of your building in terms of monthly payments. Include the costs of utilities and maintenance.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

INFORMATION SHEET

Objective 6.2: Identify the equipment needs for a business.

A. The term equipment includes those items necessary to complete the selling and non-selling functions of a business, excluding the building, people, and merchandise or materials. The entrepreneur should make a list of each type of equipment, number needed of each type as well as cost for each unit in order to operate that business.

B. Most businesses require office equipment such as chairs, desks, office machines, and filing cabinets. Sales equipment like cash registers and display racks are necessary for the retail and service businesses. Delivery trucks and conveyor belts are common necessities of wholesale and manufacturing firms.

C. The next decision for equipment will be whether to purchase or lease the equipment. Equipment (e.g., electronic computers), machinery, cars, and trucks are often leased for business use.

D. Compared to purchasing, leasing makes it possible to obtain equipment with less cash in the beginning. Lease payments, of course, must be made regularly throughout the life of the lease. A disadvantage is the typically higher total cost of leasing rather than purchasing.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION

Objective 6.2: Identify the equipment needs for a business.

A. What are some of the various types of equipment needed for a:

(1) Retail Business?

(2) Service Business?

(3) Wholesale Business?

(4) Manufacturing Business?

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION (Con't)

Objective 6.2: Identify the equipment needs for a business.

B. What are the advantages and disadvantages of leasing equipment? Purchasing equipment?

LEASING EQUIPMENT

ADVANTAGES	DISADVANTAGES

PURCHASING EQUIPMENT

ADVANTAGES	DISADVANTAGES

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

STUDENT ACTIVITIES

Objective 6.2: Identify the equipment needs for a business.

Develop a list of the various types and amounts of equipment needed for your business. Include the costs of each. Service a business similar to what you plan to open as a source of information.

Type of Equipment	Number Needed	X Unit Cost	= Cost
		$	$
		$	$
		$	$
		$	$
		$	$
		$	$
		$	$

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

INFORMATION SHEET

Objective 6.3: Determine the most effective physical layout for a business.

A. Entrepreneurs who fail to realize the importance of an effective building layout may be getting only a small part of their potential business. The most effective layout is one that uses the available space wisely. Location is the key factor. For example, the retail merchant will place impulse goods in high traffic areas of the retail store.

An analysis of the functions of the business at hand is necessary. In manufacturing, production is the key function. In retailing, customers flow to maximize sales is of primary concern. No matter what the business at hand, certain factors need to be considered:

1. Efficient use of equipment
2. Location of materials or merchandise
3. Maximum use of the building itself
4. Always keep in mind what you have to work with:
    a. People
    b. Equipment
    c. Building
    d. Goods

B. Retail Stores -- The interior plan or layout of your building should be considered from the customer's viewpoint as well as the cost of the layout. Similar lines of goods are grouped to save the customer time and energy and for ease of selling the merchandise. Items for which a customer makes special trips are often placed in the back or upper floor of the store. Also in the back of the store are the activities of receiving, marking, and offices because the space nearest the entrance has the potential for the greatest percentage of sales. Consequently as you move away from the entrance the percentage decreases.

Feature goods are displayed in outside windows and do not need to be located in the space near the entrance. Impulse goods should be placed near the entrance. Staple goods can be located in a permanent less traffic area.

In addition to standard selling fixtures, four arrangements may be used for special fixtures:

1. An aisle table, portable cart or stacking can display specials.
2. A merchandise island provides quick handling of sales and the protection of goods.
3. Merchandise can be stacked at the end of unrelated aisles.
4. Self-service aisles provide easy access of all merchandise.

There should be a certain amount of flexibility of your store layout in order to adjust to seasons, customer traffic or a new look. Counters are usually placed perpendicular to the main aisles, however, in the modern stores main aisles have gentle curves for better distribution of traffic.

C. Service Businesses -- Primary concern should be given to customer convenience. For example, a motel must consider parking, ease of entrance to rooms, and availability to recreational facilities.

D. Wholesaling -- The primary functions of a wholesaler is storage and order filling. The most efficient method of storing goods so that they are easily accessible when an order is to be filled is of primary concern.

E. Manufacturing -- The function of manufacturing is production. Various phases of production from assembly to shipping usually take place and this is what should dictate how a plant will be laid out.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION

Objective 6.3: Determine the most effective physical layout for a business.

A. What are some of the factors necessary to consider when arranging the equipment in a building?

B. What are the major objectives of a:

(1) Retail Business?

(2) Service Business?

(3) Wholesale Business?

(4) Manufacturing Business?

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION (Con't)

Objective 6.3: Determine the most effective physical layout for a business.

C. What layout factors influence each of the above businesses?

(1) Retail Business

(2) Service Business

(3) Wholesale Business

(4) Manufacturing Business

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

STUDENT ACTIVITIES

Objective 6.3: Determine the most effective physical layout for a business.

Prepare a diagram of the layout for your business by investigating the layout of businesses similar to yours. Also contact equipment, furniture and fixture manufacturers or distributors for layout assistance.

Use graph paper to complete your diagram.

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

INFORMATION SHEET

Objective 6.4: Describe the necessary criteria needed to create an effective business image through the physical appearance of the building and layout.

A. Your Building's Appearance -- What people see as they pass by the store or building is an important element in its image. Even people who never enter a store or building form an impression from its outside appearance. That impression may be the reason they don't break their stride when they go by your place of business.

B. Inside the building the layout and the decor reinforce customers' impressions about your products and salespeople. For example, fixtures which are classic in design usually appeal to older and more conservative groups. Very plain, inexpensive-appearing fixtures help to build an image with young families whose incomes are limited. Low ceilings may make the store more personal, and indirect lighting usually makes the customer think of higher quality. Some color schemes are more masculine than others.

C. Suggestion -- The outside appearance of your building should attract potential customers as well as be appealing to your present customers. Inside the building, the fixtures, layout, and displays should create an atmosphere in which the customer will feel "at home."

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

QUESTIONS FOR DISCUSSION

Objective 6.4: Describe the necessary criteria needed to create an effective business image through the physical appearance of the building and layout.

A. How important is the physical appearance of a building for customer attraction?

B. What type of image does a business want to depict through its building and layout for each of the following:

(1) Retail Business

(2) Service Business

(3) Wholesale Business

(4) Manufacturing Business

UNIT 6.0

BUILDING, EQUIPMENT AND LAYOUT

STUDENT ACTIVITIES

Objective 6.4: Describe the necessary criteria needed to create an effective business image through the physical appearance of the building and layout.

From the drawing of your building for Objective 6.1, describe in detail the physical appearance of your building and image it should project.

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

OBJECTIVES

After completing this unit, the student will be able to:

Objective 7.1	Identify the necessary operating permits and licenses needed to start a business.
Objective 7.2	Describe the tax liability of a business.

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

INFORMATION SHEET

Objective 7.1: Identify the necessary operating permits and licenses needed to start a business.

A. License -- Permit granted by the government (federal, state or local) to a person or business to engage in a business activity. Licensing is used as a source of revenue for the government and as a means of business regulation.

B. Revenue -- Money to operate a government.

C. The relationship between government and entrepreneurship can become quite controversial. Generally government regulation is utilized to protect the consumer as well as the business.

Any business that engages in interstate commerce is subjected to federal regulation. State regulations vary from state to state. Some of the more common regulations include zoning ordinances, fire laws, and minimum pricing.

D. Every business operates in a specific location. Therefore, that business must abide by the zoning laws, building codes, health codes and various other permits required by the local government.

The following list is an example of the various permits and licenses necessary to operate a business in Maricopa County and the City of Phoenix. Regardless of where your business may be located, the local city council or planning agency will be helpful in providing information for local community regulations.*

MARICOPA COUNTY. In general, Maricopa County has jurisdiction in those matters that are not specifically handled by the Incorporated Communities regarding businesses located within the County.

1. Building Permits are issued by the Department of Building Safety. For information call: 262-3694
2. Business Licenses are NOT required by Maricopa County. (See City of Phoenix - below)
3. Health Regulation, permits and inspections are handled by the Health Department. For information call: 258-6381
4. Liquor Tax is handled by the Clerk of the Board of Supervisors. For information call: 262-3766

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*"Preliminary Points to Consider in Planning a Business of Your Own" (Phoenix, Arizona: Small Business Administration), pp. 1-13.

5. Peddler's Licenses (for selling house to house or on the streets) are handled by the Sheriff's Department. For information call: 262-3136

6. Registration of a business is handled by the Recorder's Office. For information call: 262-3535

7. Signs -- Permits to erect signs are issued by the Department of Planning and Zoning. For information call: 262-3740

8. Zoning Regulations and Zoning Changes are handled by the Department of Planning and Zoning. For information call: 262-3740

CITY OF PHOENIX. The information given below only applies if your projected business will actually be located within the City Limits. If the site is in an incorporated community (other than Phoenix) local rules will apply and proper telephone numbers can be found in the Telephone Directory.

1. Business Licenses: For information call: 262-4809

2. Construction Permits. For information call the Building Safety Department: 262-7884

3. Liquor Taxes -- for information call: 262-4809

4. Sales Taxes -- for information call: 262-6785

5. Signs -- for information call: 262-7825

6. Use Taxes (Out of State purchases that have not paid Arizona State Sales Tax). For information call: 262-6860

7. Zoning -- for information call: 262-7844

The following is a partial list of regulatory licenses issued listed by title and amount of license fee. This is general information and for illustration purposes only. See the procedure book for ordinance definition, application procedure, and fee pro-ration. Fees subject to change.

TITLE	LICENSE FEE	RENEWAL INTERVAL	REMARKS
Auctioneer	$100.00 per year	Annual/Calendar	
Bowling Alley	$ 18.00 per lane	Annual/Fiscal	
Christmas Tree Lot	$ 5.00 per lot	none	$ 50.00 trust deposit
Flower Locations	$ 10.00 per corner (renewal)	Annual/Calendar	C-1, C-2 areas in City
Vending machines:			
Sidewalk	$ 25.00 annually		Downtown only
Street	$ 10.00 annually		Not Downtown

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

QUESTIONS FOR DISCUSSION

Objective 7.1: Identify the necessary operating permits and licenses needed to start a business.

A. In what ways do government regulations and requirements restrict business activity:

(1) Federal level?

(2) State level?

(3) Local level?

B. What is OSHA? Why is it important to a business?

C. Why are government regulations necessary for business?

D. Should there be a local government regulation concerning business participation in community affairs?

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

STUDENT ACTIVITIES

Objective 7.1: Identify the necessary operating permits and licenses needed to start a business.

For your business, complete the following:

1. List the required licenses or permits.

2. Describe the local zoning law requirements as to your location.

3. List all applicable building codes.

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

INFORMATION SHEET

Objective 7.2: Describe the tax liability of a business.

The tax liability of a business is dependent on the local type of business organization you choose. It is best to secure a lawyer or accountant to explain the various taxes you will have to pay. These are five general types of tax liabilities:

A. Income Tax -- As with individual income tax, sole proprietors and partners must comply with this tax liability. In addition, corporations also pay taxes. The investment tax credit deals with the purchasing of certain types of equipment.

B. Employment Tax -- This area of taxes include Social Security, Income tax withheld from employees, and Unemployment and Disability.

C. Sales Taxes -- Many state governments place a sales tax on merchandise sold as a source of state revenue.

D. Property Taxes -- Taxable property includes land, building, equipment and tools, fixtures and inventory.

E. Excise Taxes -- A federal tax placed on certain items such as alcohol, tobacco, cars, and gasoline.

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

QUESTIONS FOR DISCUSSION

Objective 7.2: Describe the tax liability of a business.

A. What are some alternatives, besides taxation, for governments to raise money?

B. How are federal taxes spent by the U.S. government?

UNIT 7.0

OPERATING PERMITS, LICENSES AND TAX REGULATIONS

STUDENT ACTIVITIES

Objective 7.2: Describe the tax liability of a business.

For your business, list the various taxes you will be responsible for. Include Federal, State and Local tax liabilities. Place this list with your list for Objective 7.1.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

OBJECTIVES

After completing this unit, the student will be able to:

Objective 8.1	Describe the function of Personnel Management.
Objective 8.2	Prepare job descriptions for positions within a business.
Objective 8.3	Determine factors to consider for Recruitment and Selection of personnel.
Objective 8.4	Using a questionnaire on training programs, define the objective to be achieved for developing a Training Program.
Objective 8.5	Prepare an organizational chart for a business.
Objective 8.6	State employee policies on Fringe Benefits, Compensation, Transfers and Promotions.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

INFORMATION SHEET

Objective 8.1: Describe the function of Personnel Management.*

A. Personnel Management is concerned with the effective use of the skills of people. They may be salespeople in a store, clerks in an office, operators in a factory, or technicians in a research laboratory. In business, it starts with the recruiting and hiring of qualified personnel and continues with directing and encouraging their growth as they encounter problems and tensions that arise in working towards goals which they did not set.

In addition to recruiting and hiring, some of the responsibilities of personnel management are:

1. To classify jobs and prepare wage and salary scales
2. To counsel employees
3. To deal with disciplinary problems
4. To negotiate with labor unions and service union contracts
5. To develop safety standards and practices
6. To manage benefit programs, such as group insurance, health, and retirement plans
7. To provide for periodic reviews of the performance of each individual employee, and for recognition of his or her strengths and needs for further development
8. To assist individuals in their efforts to develop and qualify for more advanced jobs
9. To plan and supervise training programs, and
10. To keep abreast of developments in personnel management.

B. Insights into the personnel manager's job are provided by the following examples of employee situations that are challenging:

1. The firm's employees -- especially the most qualified ones -- can get comparable, if not better, jobs with other employers.

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*Adapted from "Personnel Management" (Washington, D.C.: Small Business Administration), Small Business Bibliography No. 72.

2. When a firm faces a scarcity of supervisory and specialized personnel with adequate experience and job capabilities, it has to train and develop its own people.

3. The cost of hiring and training employees at all levels is increasing, for instance, several thousand dollars for a salesperson. A mistake in hiring or in slow and inefficient methods of training can be costly.

4. Personnel managers must comply with the law by employing, training, and promoting women and persons from minority groups. The problem in doing so is that many of these employees have not had appropriate experience and education in the past.

5. Most employees, whether or not represented by labor unions, continue to seek improvements in direct compensation, employee benefits, and working conditions. All commitments must be based upon what the firm can afford, comply with current practices of other employers, and be understood and accepted by the employee. To do this, all employee policies and operating procedures should be developed and negotiated with care.

6. Some employees may not perform satisfactorily just because their firm offers competitive compensation, benefits, and working conditions. In addition to these financial or physical compensations, they want responsibility, the opportunity to develop, and recognition of accomplishment in their jobs.

C. Personnel management works to achieve practical solutions to such problems. In large firms, it generally provides support to line management. In this staff capacity, the personnel department has the responsibility to develop and implement policies, procedures, and programs for recruitment, selection, training, placement, safety, employee benefits and services, compensation, labor relations, organization planning, and employee development.

Often, the owner-manager of a small firm also has to be a personnel manager. In such case it is necessary to have an overview of current trends and practices in personnel management.

For day-to-day reference in solving personnel problems, the owner-manager should have one or more of the current books that cover the whole field of personnel management. In addition, regular reading should include one or more magazines that devote at least part of their contents to personnel management subjects.

The individual whose only responsibility is personnel management should have in-depth knowledge of current practices and trends in this field. There is a need to be knowledgeable in personnel matters as related to his or her specific line of responsibilities.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

QUESTIONS FOR DISCUSSION

Objective 8.1: Describe the function of Personnel Management.

A. What are some ways to build and maintain employee morale?

B. Why is the human factor so important to a:

(1) Small Business?

(2) Large Business?

C. What might result from poor personnel management policies?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

STUDENT ACTIVITIES

Objective 8.1: Describe the function of Personnel Management.

Interview a personnel manager of a medium size to large business similar to the business you plan to start. Find out what their function is at that business and develop a task analysis of the position for your business.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

INFORMATION SHEET

Objective 8.2: Prepare job descriptions for positions within a business.

HOW TO WRITE A JOB DESCRIPTION*

Job Description:

A job description is a summary of the important facts about a particular job. It tells: (1) the duties, (2) how these duties are to be performed, (3) the skills needed to do the work, and (4) why the job is necessary--for example, how it ties in with the other jobs in your business.

"I'm not supposed to do that work," one employee complained to another at lunch time. "After all, I was hired as a mechanic."

At the other end of the shop, their boss was getting an earful from the owner-manager. "You've got to finish this work on time," he said.

"I know that," the foreman replied. "But it's not easy with this bunch of prima donnas. They drag their feet when I pull them away from their regular work and put them where they can help move production."

In another small plant, the owner-manager was also pressing for production. "We've got to get this stuff shipped tonight," he said to his foreman.

"It'll push us a little, but we can make it. If I shift Bill and Steve to help break a bottleneck on polishing, that should do it."

When Bill and Steve were asked to move, they went willingly. Why?

One reason was the job descriptions which the plant used. They spelled out the fact that the job included leaving the main task to help break production tie-ups.

The owner-manager had gotten the idea of using job descriptions from a friend who ran a small shoe store. On a bulletin board in the stock room was a sheet of paper on which was written the names of the store owner and the two employees.

Under each name, the owner had listed the duties and responsibilities of each individual. "This simple job description," as the shoe store owner said, "helps all three of us to know our jobs."

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*Source: "How to Write a Job Description" (Washington, D.C.,: Small Business Administration), Small Business Administration Management Aid No. 171.

The idea behind a job description is so simple that it can be used in a three-person business or in one employing several hundred. The main difference is that more information has to be gathered and used in the larger organization.

What is a Job Description?

The shoe store owner and the small plant owner-manager use job descriptions because they realize that the success or failure of their businesses is determined largely on how well employees do their own work and how well that work relates to other jobs.

Yet some owner-managers make little or no effort to identify clearly the duties of each job. Nor do they try to determine what is to be accomplished in each one. Thus when a job is poorly performed, they tend to find fault with the worker. A more logical approach might be to determine whether the worker knows what is to be done.

Depending on the work to be done, a job description can be involved or simple. It is a written record of: (1) the duties, (2) the responsibilities, and (3) the requirements of a particular job.

A description includes a summary of the significant facts pertaining to a job. These facts give the owner-manager and the employee a general understanding of: (1) what the worker does, (2) how it is to be done, and (3) why the worker does it. They also indicate the skills and responsibilities involved and its relationship to other jobs in the plant.

"What is my job?" is the question which a job description should answer clearly.

Keep in mind that a description is concerned only with the basic requirements of the job, not how well a certain individual now performs it. You will want to make this point clear because employees erroneously think that a job description is used to rate individual performance. Teach them that it is only a means of analyzing and describing the actual content of the job itself.

Three things are necessary in order to write a job description. They are: (1) convincing employees of its value, (2) preparing forms which make for easy recording of necessary facts, and (3) collecting information about the job.

Convincing Employees

The amount of convincing which you'll need to do depends on your type of work, the organization of your business, and, particularly, on the number of workers you employ. Basically, educating employees, including your foreman and other supervisors, is a communications problem.

Tell employees about your plan--individually or in small groups. Point out how job descriptions can help each employee get more satisfaction from the work. Emphasize the fact that the purpose of the description is to give understanding of what they are expected to do. It is not designed to evaluate or speed up their work.

Preparing Forms

You will need five kinds of facts to develop a description: (1) facts which identify the job, (2) facts about the skills required to do it, (3) facts about its responsibilities, (4) facts about the effort demanded by it, and (5) facts about working conditions.

An easy way to pin down this information is using a separate form for each type of facts. Look for a few moments at how the model job description forms on the following pages can be used to capture the necessary information. You may want to modify them to fit your own needs.

Form 1. Use it to capture identification facts, such as: (1) job title and code number, (2) location of job, (3) number of employees on the job, (4) salary, (5) working hours, and (6) miscellaneous.

Form 2. Use it to jot down facts about skill requirements, such as: (1) educational requirements, (2) job experience, and (3) relation to other jobs, (4) job duties, and (5) job knowledge.

Form 3. Use it to note facts about responsibilities, such as: (1) direction and group leadership, (2) business operation, (3) care of equipment, (4) safety and health of others, and (5) contact with public.

Form 4. Use it to pin down facts about the effort which the job demands.

Form 5. Use it to note the working conditions of the job.

Collecting the Information

Your employees can supply much of the information which you need for writing the job descriptions. The employees working on a particular job know their duties during the day. They also know the responsibilities which go with those duties.

When establishing a new job, you should write the best description you can and let an employee test it. The employee can help you revise the description to fit the conditions that develop in the test period.

In a small plant, the interview method is the best to get these facts. Talk directly to the employee about the job. Of course, it takes time to get the information, but an advantage is accuracy. You are more apt to get a true picture of what is involved in the job when you and the employee engage in a "give and take" discussion of it.

If you decide to use a conference with a group of employees who work on the same job or a questionnaire which employees fill out, keep in mind the fact that each had disadvantages. In the conference method, shy employees are not apt to speak up. And some of these reserved employees may know more about the job than the boisterous talkers who dominate the meeting.

The questionnaire method has two disadvantages. First, you have to work out the questions and get them typed up. And second, even the best-thought-out questions might not mean the same thing to each employee. The result, of course, is inaccurate and conflicting information.

Above all, bear in mind that the information you collect about a job must be factual and accurate.

Using the Job Description

After you have collected the data from each employee you can begin to use the job description by:

(1) Giving the employee a copy.

(2) Making sure that the employee does the job as described.

(3) Using the description as a guide when hiring a new employee. It also helps the applicants determine whether they want the job.

And finally, be sure to make out a description on your own job. The exercise may show up ways to make your own work easier.

Form 1

IDENTIFICATION FACTS

Job Title ______________________ Location ______________________

Other titles used ______________________ Number employed: M __________ F __________

Brief summary of nature or function of job* ______________________

____

Code number** __________

Salary range: Minimum ______________________ Maximum ______________________

Average bonus or incentive payment ______________________

Working hours: Shift: __________ From __________ To __________

Overtime: ______ never ______ seldom ______ frequent; average hours per week: ______

Misc. ______________________

*A 1-sentence description, to give a general idea of job.

**Job definition (from the *Dictionary of Occupational Titles*; your local State Employment Service Office can be helpful.)

Form 2

SKILL REQUIREMENTS

Educational Requirements: (general education--grade or years)

Grammar School ____________ High School ____________ Business School ____________ College ____________

Specific education for job ____

Job Experience:

Previous experience required: None ________

Acceptable type and length ____

Average length of time with organization ________________________________

Previous jobs normally held ____

Next job in line of promotion ____

Relation to Other Jobs: Contacts regularly as part of job:

Within the Company ____________________ Outside the Company ____________________

Exercises Supervision Over:

Position of individual: ____

Subject of supervision: ____

Is Supervised by:	Position of individual	Subject of supervision
Immediate supervisor	____________	____________
Others	____________	____________

Job Duties:

Regular:

Before open for business ____

During business hours ____

After business hours ____

Periodic (weekly or monthly):

Performed on regular time ____

Performed after hours ____

Occasional: Performed on regular time ________________________________

Performed after hours ________________________________

Job Knowledge:

General ____________ Policies and Regulations Special and Departmental ____________

Procedures and Methods

____________ ____________

Technical Information ____________ Related Information ____________

Use of equipment: Types of equipment: ________________________________

Special operations ____

Form 3

RESPONSIBILITIES

Direction & Group Leadership:

None ______ Occasional ______ Frequent ______ Continual ______

Nature of responsibility ______________________________

Business Operation:

None ______ Occasional ______ Frequent ______ Continual ______

Nature of responsibility ______________________________

Care of Equipment:

None ______ Occasional ______ Frequent ______ Continual ______

Nature of responsibility ______________________________

Safety and Health of Others:

None ______ Occasional ______ Frequent ______ Continual ______

Nature of responsibility ______________________________

Contact with Public: None ______ Occasional ______ Frequent ______ Continual ______

Form 4

EFFORT DEMAND

Physical Activities

- ____ Standing
- ____ Walking
- ____ Balancing
- ____ Climbing
- ____ Turning
- ____ Running
- ____ Stooping
- ____ Sitting
- ____ Reaching
- ____ Throwing
- ____ Lifting
- ____ Carrying
- ____ Pushing
- ____ Pulling
- ____ Fingering
- ____ Feeling
- ____ Smelling
- ____ Testing
- ____ Hearing
- ____ Seeing

Worker Characteristics

- ____ Planning
- ____ Directing others
- ____ Writing
- ____ Showing enthusiasm
- ____ Being well groomed
- ____ Controlling emotions
- ____ Using arithmetic
- ____ Working accurately
- ____ Discriminating colors
- ____ Talking
- ____ Showing initiative
- ____ Getting along with people
- ____ Working at various tempos
- ____ Concentrating amid distractions
- ____ Remembering names and faces
- ____ Remembering details
- ____ Examining and observing details
- ____ Attending to many items
- ____ Making decisions
- ____ Working rapidly

Form 5

WORKING CONDITIONS

- ____ Inside
- ____ Outside
- ____ Humid
- ____ Hazards
- ____ High places
- ____ Change of temperature
- ____ Hot
- ____ Cold
- ____ Dry
- ____ Wet
- ____ Dirty
- ____ Dusty
- ____ Odors
- ____ Noisy
- ____ Inadequate light
- ____ Inadequate ventilation
- ____ Working with others
- ____ Working around others
- ____ Working alone
- ____ Working under pressure

Details of Working Conditions (summary based on working conditions) ______________________________

Details of Hazards ______________________________

Permissible Handicaps: Limb ____ Hearing ____ Sight ____

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

QUESTIONS FOR DISCUSSION

Objective 8.2: Prepare job descriptions for positions within a business.

A. What are some alternative methods of collecting information for a job description besides using your own employees?

B. What intrinsic value would take place by asking an employee for input to prepare a job description?

C. How could job descriptions be used to aid employees in developing long-range goals?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

STUDENT ACTIVITIES

Objective 8.2: Prepare job descriptions for positions within a business.

Prepare a job description for yourself within your business and at least two other major positions within that business. If you are developing a sole proprietorship, project future expansion of your company for the other two major positions.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

INFORMATION SHEET

Objective 8.3: Determine factors to consider for Recruitment and Selection of personnel.

A. Recruitment -- The major factor to consider in recruitment is locating candidates. It has been proven that one will be more successful if an active method of recruitment is initiated as opposed to waiting for employment applications to walk in. Locating possible candidates may come from any of the following methods:

1. Walk ins -- people who walk in to inquire about job possibilities
2. Informal sources, such as trade groups, high school teachers, college teachers, and professional schools
3. Classified ads
4. Private or public employment agencies

B. Selection -- Four major steps are considered when selecting a candidate:

1. Resume and application
2. Employment tests
3. The interview
4. Checking references

Criteria for each of these areas should be initiated to make the selection procedure consistent for all applicants.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

QUESTIONS FOR DISCUSSION

Objective 8.3: Determine factors to consider for Recruitment and Selection of personnel.

A. Why would an active recruitment procedure be more beneficial to an entrepreneur than waiting for walk-ins?

B. What basic step should an employer take before an applicant is selected?

C. Are employment tests worthwhile for the small entrepreneurship?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

STUDENT ACTIVITIES

Objective 8.3: Determine factors to consider for Recruitment and Selection of personnel.

1. Develop a classified ad for one position within your company. (Use the job description developed for Objective 8.2).

2. For that position, develop the criteria you would use for selecting a candidate for the above position.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

INFORMATION SHEET

Objective 8.4: Using a questionnaire on training programs, define the objective to be achieved for developing a Training Program.

Various stages of training are necessary in order to develop the type of employee who will benefit your concern. Below are a series of questions designed to provide a step-by-step approach to the task of organizing and conducting a successful program of employee training.*

Implement the checklist as a guide. The experience of other companies in training can provide additional guides. Keep in mind the training needs of your particular situation.

What is the Goal of the Training?

The questions in this section are designed to help the owner-manager in defining the objective or goal to be achieved by a training program. Whether the objective is to conduct initial training, to provide for upgrading employees, or to retrain for changing job assignments, the goal should be spelled out before developing the plan for the training program.

	Yes	No
1. Do you want to improve the performance of your employees?	______	______
2. Will you improve your employees by training them to perform their present tasks better?	______	______
3. Do you need to prepare employees for newly developed or modified jobs?	______	______
4. Is training needed to prepare employees for promotion?	______	______
5. Is the goal to reduce accidents and increase safety practices?	______	______
6. Should the goal be to improve employee attitudes especially about waste and spoilage practices?	______	______
7. Do you need to improve the handling of materials in order to break production bottlenecks?	______	______

*Source: "Checklist for Developing a Training Program" (Washington, D.C.: Small Business Administration), Small Business Administration Management Aid No. 186.

	Yes	No
8. Is the goal to orient new employees to their jobs?	_____	_____
9. Will you need to teach new employees about overall operation?	_____	_____
10. Do you need to train employees so they can help teach new workers in an expansion program?	_____	_____

What Does the Employee Need to Learn?

Once the objective or goal of the program is set, you will need to determine the subject matter. The following questions are designed to help you decide what the employee needs in terms of duties, responsibilities, and attitudes.

	Yes	No
11. Can the job be broken down into steps for training purposes?	_____	_____
12. Are there standards of quality which trainees can be taught?	_____	_____
13. Are there certain skills and techniques which trainees must learn?	_____	_____
14. Are there hazards and safety practices which must be taught?	_____	_____
15. Have you established the methods which employees must use to avoid or minimize waste and spoilage?	_____	_____
16. Are there materials handling techniques that must be taught?	_____	_____
17. Have you determined the best way for the trainees to operate the equipment?	_____	_____
18. Are there performance standards which employees must meet?	_____	_____
19. Are there attitudes that need improvement or modification?	_____	_____
20. Will information on your products help employees to do a better job?	_____	_____
21. Should the training include information about the location and use of tool cribs and so on?	_____	_____
22. Will the employee need instruction about departments other than his own?	_____	_____

What Type of Training?

The type of training to be offered has an important bearing on the balance of the program. Some types lend themselves to achieving all of the objectives or goals, while others are limited. Therefore you should review the advantages of each type in relation to your objective or goal.

	Yes	No
23. Can you train on-the-job so that employees can produce while they learn?	______	______
24. Should you have classroom training conducted by a paid instructor?	______	______
25. Will a combination of scheduled on-the-job training and vocational classroom instruction work best for you?	______	______
26. Can your goal be achieved with a combination of on-the-job training and correspondence courses?	______	______

What Method of Instruction?

One or more methods of instruction may be used. Some are better for one type of training than another: for example, lectures are good for imparting knowledge, and demonstrations are good for teaching skills.

	Yes	No
27. Does the subject matter call for a lecture, or series of lectures?	______	______
28. Should the instructor follow up with discussion sessions?	______	______
29. Does the subject matter lend itself to demonstrations?	______	______
30. Can operating problems be simulated in a classroom?	______	______
31. Can the instructor direct trainees while they perform the job?	______	______

What Audio-Visual Aids Will You Use?

Audio-visual aids help the instructor to make his/her points and enable the trainees to grasp and retain the instructions.

	Yes	No
32. Will a manual of instruction--including job instruction sheets--be used?	______	______

	Yes	No
33. Will trainees be given an outline of the training program?	______	______
34. Can outside textbooks and other printed materials be used?	______	______
35. If the training lends itself to the use of motion pictures, film strips or slides, can you get ones that show the basic operation?	______	______
36. Have you drawings or photographs of the machinery, equipment or products which could be enlarged and used?	______	______
37. Do you have miniatures or models of machinery and equipment which can be used to demonstrate the operation?	______	______

What Physical Facilities Will You Need?

The type of training, the method of instruction and the audio-visuals will determine the physical facilities needed for the training. In turn, the necessary physical facilities will determine the location of the training. For example, if a certain production machine is necessary, the training would be conducted in the shop.

	Yes	No
38. If the training cannot be conducted on the production floor, do you have a conference room or a lunch room in which it can be conducted?	______	______
39. Should the training be conducted off the premises, as in a nearby school, restaurant, hotel or motel?	______	______
40. Will the instructor have the necessary tools, such as a blackboard, lectern, film projector, and a microphone (if needed)?	______	______
41. Will there be sufficient seating and writing surfaces (if needed) for the trainee?	______	______
42. If equipment is to be used, will each trainee be provided with his own?	______	______

What About the Timing?

The length of the training program will vary according to the needs of your company, the material to be learned, the ability of the instructor, and the ability of the trainees to learn.

	Yes	No
43. Should the training be conducted part-time and during working hours?	_____	_____
44. Should the sessions be held after working hours?	_____	_____
45. Will the instruction cover a predetermined period of time? (For example, 4 weeks, 6 weeks, 3 months.)	_____	_____
46. Can the length of each session and the number of sessions per week be established?	_____	_____

Who Will be Selected as Instructor?

The success of training depends to a great extent on the instructor. A qualified one could achieve good results even with limited resources. On the other hand, an untrained instructor may be unsuccessful even with the best program. You may want to use more than one person as instructor.

	Yes	No
47. Can you fill in as an instructor?	_____	_____
48. Do you have a personnel manager who has the time and the ability to do the instructing?	_____	_____
49. Can your foreman or department heads handle the instruction?	_____	_____
50. Should a skilled employee be used as the instructor?	_____	_____
51. Will you have to train the trainer, if he/she is an employee?	_____	_____
52. Is there a qualified outside instructor available for employment on a part-time basis?	_____	_____

Who Should be Selected?

Employees should be selected for training on the basis of the goal of the program as well as their aptitudes, physical capabilities, previous experiences, and attitudes.

	Yes	No
53. Should new employees be hired for training?	_____	_____
54. Should the training of new employees be a condition of employment?	_____	_____
55. Would you prefer trainees with previous experience in the work?	_____	_____

	Yes	No
56. Are there present employees who need training?		
57. Will you consider employees presently in lower rated jobs who have the aptitude to learn?		
58. Is the training to be a condition for promotion?		
59. Will the training be made available to handicapped employees whose injury occurred while employed by the company?		
60. Will employees be permitted to volunteer for the training?		
61. Should employees displaced by job changes, departmental shut-downs, automation, and so on be given the opportunity to be trained in other jobs?		

What Will the Program Cost?

It may be desirable to compute the costs of your training before starting the program. Thus, you can budget sufficient funds for the program and use the budget as a tool for keeping training costs in line.

	Yes	No
62. Should you charge the program for the space, the machines, and materials used?		
63. Will the wages of trainees be included?		
64. If the instructor is an employee, will his/her pay be included in the costs?		
65. Will the time you and others spend in preparing and administering the program be part of the costs?		
66. If usable production results from the sessions, should the results of it be deducted from cost of the program?		

What Checks or Controls Will You Use?

The results of the training program need to be checked to determine the extent to which the original goal or objective was achieved.

	Yes	No
67. Can you check the results of the training against the goal or objective?		
68. Can standards of learning time be established against which to check the progress of the trainees?		

		Yes	No
69.	Can data on trainee performance be developed before, during, and after training?	_____	_____
70.	Will records be kept on the progress of each trainee?	_____	_____
71.	Will trainees be tested on the knowledge and skills acquired?	_____	_____
72.	Will the instructor rate each trainee during, and at the end of, the course?	_____	_____
73.	Will the trainee be followed up periodically be his/her foreman or department head to determine the long-range effects of his/her training?	_____	_____
74.	Should you personally check and control the program?	_____	_____

How Should the Program be Publicized?

Publicizing the company's training program in the community helps attract qualified job applicants. Publicity inside the company helps motivate employees to improve themselves.

		Yes	No
75.	If the program is announced to employees, will the announcement be made before the program starts? During the program?	_____	_____
76.	Are pictures to be taken of the training sessions and used on bulletin boards and in local newspapers?	_____	_____
77.	Should employees who complete the training be awarded certificates?	_____	_____
78.	Should the certificates be presented at a special affair, such as a dinner?	_____	_____
79.	When the certificates are awarded, will you invite the family of the trainees?	_____	_____
80.	Should the local newspaper, radio, and TV people be invited to be the "graduation" exercises?	_____	_____

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

QUESTIONS FOR DISCUSSION

Objective 8.4: Using a questionnaire on training programs, define the objective to be achieved for developing a Training Program.

A. What are some alternative methods of training employees without holding formal instruction?

B. What is the short-range value of training employees? Long-range value?

C. What would you consider to be the most important phase of training and why?

(1) Orientation?

(2) Improvement?

(3) Developmental?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

STUDENT ACTIVITIES

Objective 8.4: Using a questionnaire on training programs, define the objective to be achieved for developing a Training Program.

Develop an orientation training program for all new employees. How would you implement such training?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

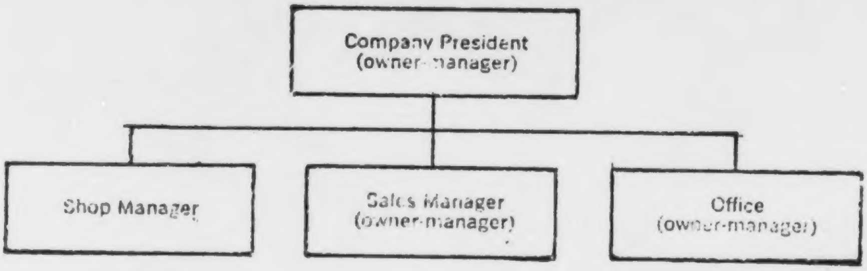
INFORMATION SHEET

Objective 8.5: Prepare an organizational chart for a business.

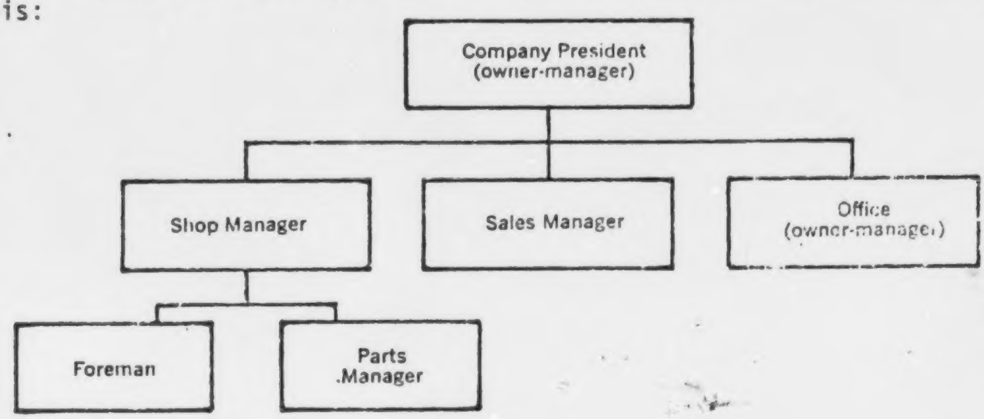
An important step in setting up a business is to find and hire capable employees. Then one must train them to work together to get the job done. Obviously, organization is needed if a business is to produce what one expects it to produce, namely profits.

Organization is essential because the owner-manager cannot do all the work. As an organization grows, one has to delegate work, responsibility and authority. A helpful tool in getting this done is the organization chart. It shows at a glance who is responsible for the major activities of a business. Examples are given in preparing an organization chart for various businesses.

A. An organization chart for a small service business will reflect the fact that the owner-manager does most of the managing himself/herself. For example, an organization chart for a small service business might look like this:*


Company President (owner-manager)
Shop Manager
Sales Manager (owner-manager)
Office (owner-manager)

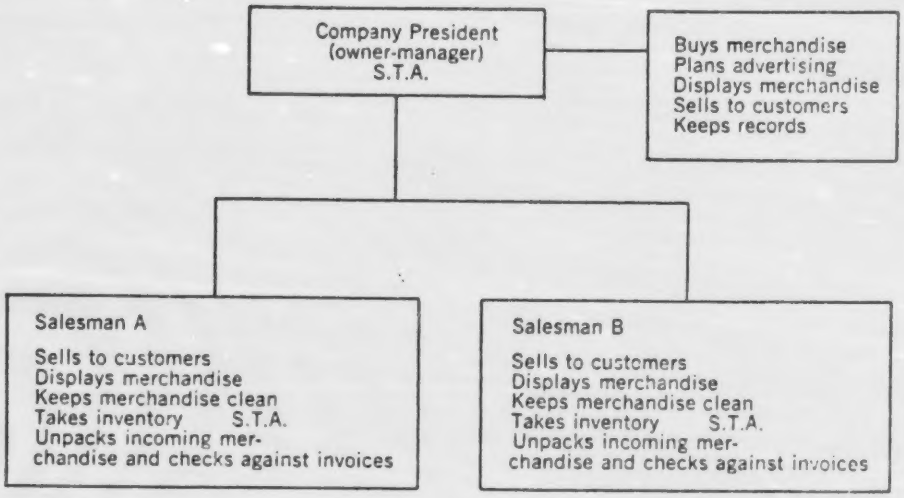
As the service business grows, its organization chart could look like this:


Company President (owner-manager)
Shop Manager
Sales Manager
Office (owner-manager)
Foreman
Parts Manager

---

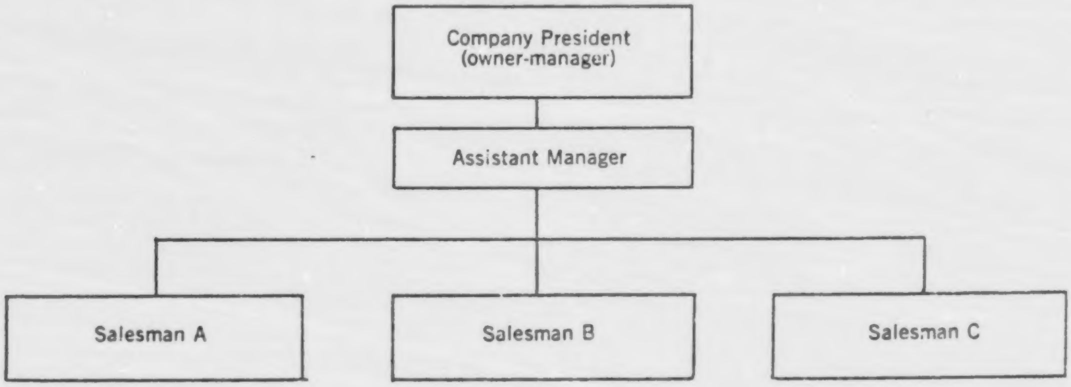
*Source: "Business Plan for Small Service Firms" (Washington, D.C.: Small Business Administration), Small Business Administration Management Aid. No. 153.

B. An organization chart for a small retail store will reflect the fact that the owner-manager does most of the managing work himself/herself. For example, if your store is run by yourself and two salespersons, the chart should show what you expect each of them to do. It could look like this: *


Company President
(owner-manager)
S.T.A.
Buys merchandise
Plans advertising
Displays merchandise
Sells to customers
Keeps records
Salesman A
Sells to customers
Displays merchandise
Keeps merchandise clean
Takes inventory S.T.A.
Unpacks incoming merchandise and checks against invoices
Salesman B
Sells to customers
Displays merchandise
Keeps merchandise clean
Takes inventory S.T.A.
Unpacks incoming merchandise and checks against invoices

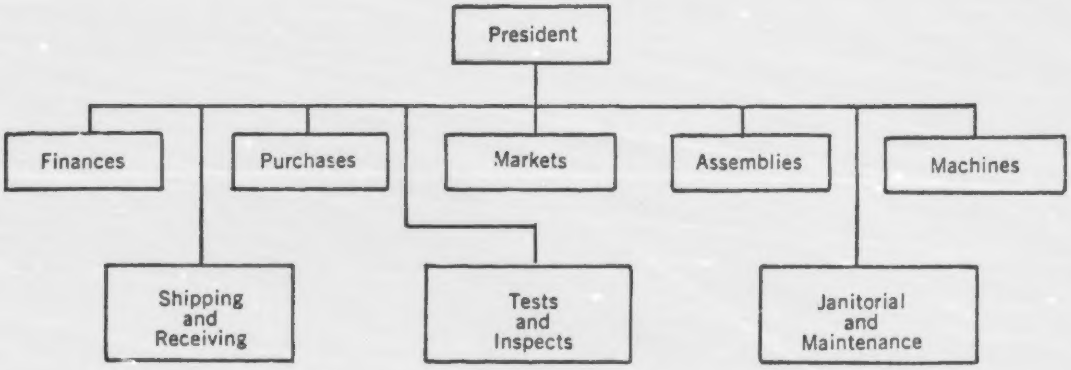
A small store exists to serve customers. They want to be served promptly and don't like to be ignored even by the stock boy. A device to insure that they are recognized is S.T.A.--Special Team Assignment. When all the salespeople are tied up, the available employee moves into Special Team Assignment.

As the business grows, the owner-manager might set up the job of Assistant Manager. The organization chart should look like this:

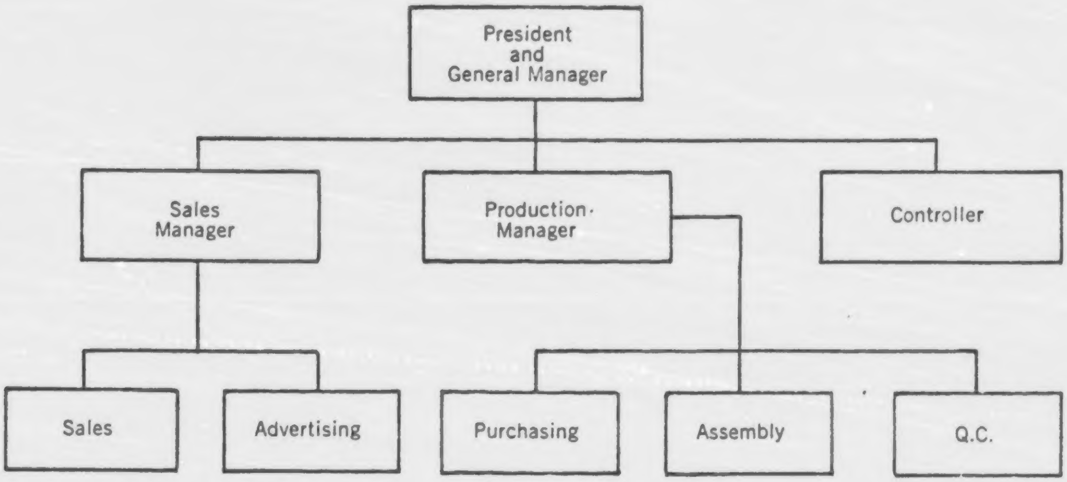

Company President
(owner-manager)
Assistant Manager
Salesman A
Salesman B
Salesman C

*Source: "Business Plan for Retailers" (Washington, D.C.: Small Business Administration), Small Business Administration Management Aid No. 150.

C. In the beginning, the president of the small manufacturing company probably does everything.*


President
Finances
Purchases
Markets
Assemblies
Machines
Shipping and Receiving
Tests and Inspects
Janitorial and Maintenance

As the company grows to perhaps 50 - 100 employees, the organization may begin to look something like the chart below.


President and General Manager
Sales Manager
Production Manager
Controller
Sales
Advertising
Purchasing
Assembly
Q.C.

*Source: "Business Plan for Small Manufacturers" (Washington, D.C.: Small Business Administration), Small Business Administration Aid No. 218.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

QUESTIONS FOR DISCUSSION

Objective 8.5: Prepare an organizational chart for a business.

A. Before a task is delegated to an employee, what necessary criteria should be considered concerning the task and the employee to carry out that task?

B. Why might it be important to show a new employee the organizational chart of one's business?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

STUDENT ACTIVITIES

Objective 8.5: Prepare an organizational chart for a business.

Using the examples of organizational charts, develop an organizational chart for your business.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

INFORMATION SHEET

Objective 8.6: State employee policies on Fringe Benefits, Compensation, Transfers, and Promotions.

Policies need to be developed in the areas of fringe benefits, compensation, transfers and promotion.

A. Fringe Benfits -- The following list gives consideration to many different areas of benefits. What benefits are chosen depends on the nature of the business at hand.

Benefits

- Vacations
- Holidays
- Group Insurance
- Hospitalization and Surgical Benefits
- Free Parking
- Training Program
- Christmas Bonus
- Savings Plan
- Profit-Sharing Plan
- Suggestion Awards
- Jury Duty
- Military Leave
- U.S. Old Age Benefits
- Unemployment Compensation
- Equal Employment Opportunity

Special Services

Credit Union

Education Plans

Medical Dispensary

Employee Purchases

Company Cafeteria

Monthly Magazine

Annual Outing

Bowling League

Baseball Team

B. Compensation -- Determinants in setting salaries and wages include:

1. The minimum wage
2. Union scales
3. Applicants previous salary and experience

Wages may be based on a set salary, an hourly rate or a commission of sales or production.

Other considerations for compensation include:

1. Work hours and over-time pay
2. Vacation and sick leave
3. Fringe benefit costs

C. Transfers and Promotions -- The use of good job descriptions and a precise organizational chart will serve as an aid in developing policies for transfers and promotions.

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

QUESTIONS FOR DISCUSSION

Objective 8.6: State employee policies on Fringe Benefits, Compensation, Transfers, and Promotions.

A. What is the difference between a transfer and a promotion?

B. What types of wage incentives might motivate an employee on a job?

C. What are some ways to build employee morale on the job?

UNIT 8.0

PERSONNEL MANAGEMENT FOR THE ENTREPRENEUR

STUDENT ACTIVITIES

Objective 8.6: State employee policies on Fringe Benefits, Compensation, Transfers, and Promotions.

1. Develop a list of fringe benefits for your business.

2. What compensation policies will you initiate for your company?

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

OBJECTIVES

After completing this unit, the student will be able to:

Objective 9.1	Define the purposes of advertising.
Objective 9.2	Prepare an advertising budget.
Objective 9.3	Select the advertising media to be used.
Objective 9.4	Determine methods of coordinating advertising with other sales promotion activities.
Objective 9.5	Identify consumer protection laws dealing with advertising.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

INFORMATION SHEET

Objective 9.1: Define the purposes of advertising.

A. Purpose of Advertising -- Advertising is important to the small businessperson because it acquaints the public with the retailer's products and the prices charged. It is necessary to note that advertising is a means to an end -- a way to inform people of the product.

Over decades businesspeople have used advertising as a means of getting their wares into the hands of consumers. In early use, shopkeepers erected signs on or in front of their stores or placed posters in public places, to draw the attention of prospective customers to their place of business.

Advertising planning begins with a discussion on specific advertising objectives. Objectives are the desired results that represent an organization's reasons for being in existence. Therefore, an advertising plan must begin with a purpose. It would be foolish to plan the how (methods) of advertising before determining who is the target and what is to be accomplished.

B. Components of Advertising -- Advertising that helps sell merchandise consists of the following elements:

1. Attention-getting copy
2. Unusual use and placement of typeface and white space for the print media
3. Interesting sound effects for radio or visual media
4. Identifying the store's position in supplying consumer goods and services
5. Encouraging word-of-mouth publicity provided by satisfied repeat customers

Once attention is gained, an ad must fill a need and convince the consumer that he will benefit from the purchase. It is important for the business to build the advertising message around a unique selling point of the product or service. For example, "the price is lower than anyone's in town," "a wider selection of colors or fabrics" or, "the best service in town."

Finally, the ad must have a call to action; invite the target audience to come in and purchase the product. Selling is a personal thing, but if the ad is good, it will draw people into the store so they can be sold.

There are four main steps to follow when creating an advertising technique:

1. Research -- find out what the product is all about and to whom the ad should be aimed. Make a checklist of the ways and areas in which you are superior to, equal to, or behind competition.

2. Strategic planning -- determine the results desired from advertising, allocation of money to the advertising budget, creative strategy, and areas of media that can be used.

3. Tactical decisions -- actual purchasing of media (newspaper space, radio/TV time).

4. Advertisement construction -- writing copy, preparing artwork and layout resulting in the finished ad.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

QUESTIONS FOR DISCUSSION

Objective 9.1: Define the purposes of advertising:

A. What is the difference between institutional and promotional advertising? Give an example of each.

B. Who uses industrial advertising? Who is it directed toward?

C. Is advertising or personal selling more important to a:

(1) Small Business?

(2) Large Business?

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

STUDENT ACTIVITIES

Objective 9.1: Define the purposes of advertising.

For your business, select a line of products or service. Then:

1. Find out what the product or service is all about and to whom an ad should be aimed.

2. Make a checklist of the ways and areas in which you are superior to, equal to, or behind competition.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

INFORMATION SHEET

Objective 9.2: Prepare an advertising budget.

Once goals have been set, money needs need to be assessed. One of the best methods to use when setting an advertising budget is the percentage of sales method. Here you set a fixed total amount for the year's advertising, then divide that amount into parts for each media selected.

Another method is the objective and task method. The goals and objectives of advertising are determined and money is allocated to best meet those needs.

A calendar approach may be used to break down the advertising budget by listing the various media to be used along with its cost and length of the ad will run.

Timing is possibly the most important single consideration in planning effective advertising. Timing involves adjusting advertising plans to the seasonal patterns of the business, to the store's special days, and to the community's special events. If the retailer, for example, is located in a college-oriented town, they should plan to advertise specials over football weekends and during other student-oriented events of the year. They should also allocate part of the budget for advertising in the school paper and other student publications.

No matter what media is used, the advertisement should be timely. An example is the campaign used by an ice cream chain. It came out with a lunar-flavored ice cream and timed its introduction with the moon landing. Stores were told not to advertise the confection until the astronauts landed on the moon. When they landed, signs then went up in store windows, and ads about the new lunar ice cream appeared in papers and on radio.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

QUESTIONS FOR DISCUSSION

Objective 9.2: Prepare an advertising budget.

A. How can the amount of money to be spent on advertising be determined by the entrepreneur?

B. In what ways do many small businesses "mis-spend" money on advertising?

C. What would be the best method to insure effective advertising?

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

STUDENT ACTIVITIES

Objective 9.2: Prepare an advertising budget.

If the usual expense for advertising in your chosen line of business were 3% of sales, would you be justified spending 5% during your first year in business? In spending 10% 20%? Give reasons why.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

INFORMATION SHEET

Objective 9.3: Select the advertising media to be used.

Before choosing the combination of media appropriate to reach the target market, the entrepreneur must define the target audience. "Who do I want as my customers? Who needs my products? Who will buy my products?" It is essential to note that advertising is just one media will not effectively reach the target market.

The primary types of advertising media include:

A. Newspapers

B. Magazines

C. Radio

D. Television

E. Direct Mail

F. Other media including billboards, transit advertising, specialty and yellow pages

A. Newspaper advertising -- There are four basic types:

1. Dailies (large metropolitan editions)

2. Special audience (tailored to an ethnic group or for resident of a certain area of a city)

3. Shoppers' news (usually distributed free of charge and designed specifically for retail advertising purposes)

4. Sunday editions (have larger circulations, contain more pages and ads - many retailers feel are read more thoroughly than dailies)

B. Magazine advertising -- Magazine advertising is basically a national media, although there are many regional magazines. Advertisements in magazines are usually aimed at a particular group of people. For instance, women's magazines primarily have ads about cosmetics, fashions, and shampoos. Sports magazines seem to have ads about athletic equipment or products that appeal to the active person. Magazines have beautiful color ads and are kept much longer than newspapers. However, advertisements in magazines are very expensive, and require as much as a month or more lead time for submitting the copy.

C. Radio advertising -- Radio advertising has remained a very important advertising source despite the invasion of television. It is estimated that every American owns at least one radio - not including car radios! People listen to the radio in the morning, at noon, at night, and to and from work. Like newspapers, radio advertisements or spots can be localized and appeal to people in certain geographic areas. Also, radio "spots" can be purchased for selected air time which allows for aiming the message to specific populations such as truck drivers in the middle of the night, housewives during the day, and farmers in the early morning.

D. Television advertising -- Television advertising is extremely important since an estimated 90 percent of the American families own a television. TV ads or commercials offer a distinct advantage over the other media because of the visual action. Viewers can see the product demonstrated, colors, sizes and beautiful models which has an influence on the viewer. Television commercials can also appeal to specific people at preselected times. Television advertising is very expensive, however.

E. Direct-mail advertising -- Direct-mail advertising is sometimes called "Junk Mail." However, much of this so-called Junk Mail contains valuable information such as catalogs, booklets and coupons. All types of advertisers use direct-mail advertising, mainly because they can choose the geographic areas in which they wish to advertise, at the time they want to advertise. The cost of direct-mail advertising per message is relatively high.

F. Other -- Transit advertising includes signs inside or mounted on the outside of buses, taxis, commuter trains, and subway cars.

Yellow Pages in the telephone directories are useful to businesses. This medium is particularly suitable for retailers who are trying to inform newcomers about their business, sell offerings that are purchased only infrequently or in emergencies, or sell merchandise for which consumers shop around and make comparisons.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

QUESTIONS FOR DISCUSSION

Objective 9.3: Select the advertising media to be used.

A. What media should be selected by the small entrepreneur?

B. What are the advantages and disadvantages of newspaper as an advertising media?

NEWSPAPER

ADVANTAGES	DISADVANTAGES

C. Is TV advertising realistic for the small entrepreneur?

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

STUDENT ACTIVITIES

Objective 9.3: Select the advertising media to be used:

Complete two of the following projects.

1. Design 2 billboards and tell where you would have them placed. (Why at that particular place?) Draw these billboards on 8 1/2 " x 11" unruled white paper.

2. Make one TV commercial lasting 10-30 seconds. Prepare a written "script" for the commercial.

3. Prepare 2 radio commercials - 10 to 30 seconds each. Prepare a written script.

4. Select a packaged product and explain the packaging and design of the product's container. Make drawings if necessary.

5. Design any other forms of possible promotion activities for this new product, such as in-store display, newspaper coupons, direct mail advertising, etc.

6. Design a magazine advertisement. Draw it on a poster board. Your magazine advertisement will be rated as follows: headline - 5 pts. copy - 5 pts. product illustration - 5 pts. signature block - 5 pts. (where to buy, manufactured by).

   Do a pencil sketch of this magazine ad first. Have it approved by your teacher. Use only 1 or 2 colors for your headline and copy. Any number of colors may be used for the rest of the ad.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

INFORMATION SHEET

Objective 9.4: Determine methods of coordinating advertising with other sales promotion activities.

Special events are specially planned and advertised events designed to promote sales or good will, built around traditional holidays, seasonal changes, and community interests. The purposes of special events are:

1. To attract people and win new customers for a business
2. To introduce new products, new departments, new branch stores, or new service or services
3. To increase volume when too slow
4. To offer special bargains to customers
5. To call special attention to a line of goods
6. To create interest during slack periods
7. To cooperate with community activities
8. To perform extra service to customers

Basically, promotion involves communication to consumers. A promotion blend consists of that combination of methods used by a business to communicate with its customers.

As with advertising and personal selling, supportive methods are intended to accomplish the general purposes of promotion: sell specific offerings, create the desired store image, and generate shopper traffic. In deciding whether to use supportive promotion or which method to use, a manager must first decide specifically what the promotion is to accomplish.

For promotion to be effective it should:

Attract Attention

Generate Interest

Create Desire

Obtain Action

in other words, AIDA.

In order to accomplish these tasks there are many forms of promotion. Below are some examples.

1. Display -- An arrangement of merchandise and information for shopper's viewing. Of the many promotional methods; display probably is the most widely used and perhaps the most significant. As the self-service approach to retailing has grown, display's overall importance in the promotion blend has increased. Since self-service means reduced personal selling, display is expected to perform part of the selling function, in fact, a major part in most self-service stores.

   There are two types of displays:

   (a) Display Windows -- Arrangement itself is in-store, although the shoppers are passing by outside the store. These displays are very important for stores with considerable pedestrian traffic. The displays are designed to attract customers into the store.

   (b) Interior Displays -- Located right in a store's selling area. With few exceptions interior displays are supposed to sell specific offerings. This purpose has grown in importance as rising incomes have permitted more frequent impulse purchases by shoppers. A Point-of-Purchase Display (POP) is a special arrangement set up beside complete stock of the item, in the spot where a customer makes a selection. Many suppliers provide retailers with free POP materials for their brands.

2. Sampling -- Issuing of free trial products.

3. Demonstrations -- Method of explaining the use of a product or service.

4. Shows -- Special events for demonstrating merchandise.

5. Spectaculars -- Some stores have very elaborate and expensive supportive promotions such as The Macys' Thanksgiving Day Parade.

6. Grand Openings -- Special promotion for the opening of a new store.

7. Publicity -- Free promotion. Includes those promotion activities with no out-of-pocket costs to a retailer. Personal appearances and news stories are the most common forms of publicity.

8. Word-of-mouth -- Publicity via customer to friends.

9. Trading Stamps -- Stamps which can be accumulated and then traded for merchandise, cash or for reductions on grocery items.

10. Premium Offers -- A product or service is given free or at a greatly reduced price with the purchase of another designated offering.

11. Coupons -- Involves distributing a certificate which entitles a person to buy a particular offering at a reduced price. Couponing can be initiated by both manufacturers and retailers.

12. Special Sales -- Merchandise with reduced prices is promoted in a vigorous manner for a limited period of time.

13. Contests -- In-store contests are competitive activities usually designed to motivate salespeople to increase productivity or sales. Customer contests are designed to motivate the customer to return to that business to shop for the chance to "win."

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

QUESTIONS FOR DISCUSSION

Objective 9.4: Determine methods of coordinating advertising with other sales promotion activities.

A. Why might sales promotion be more difficult in a manufacturing business than in a retail business?

B. How important are display windows to a retailer?

C. Is publicity worthwhile?

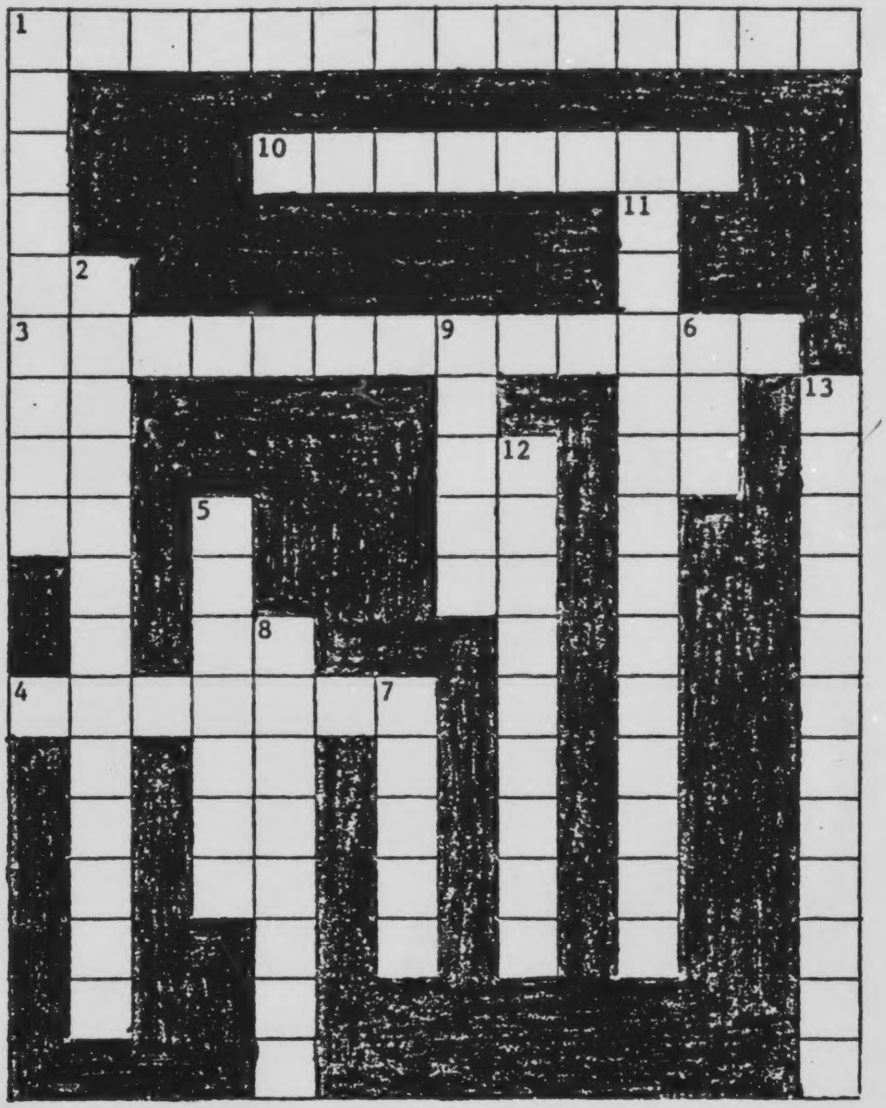
UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

STUDENT ACTIVITIES

Objective 9.4: Determine methods of coordinating advertising with other sales promotion activities.

Complete the following crossword puzzle using the definitions on the next page.



UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

STUDENT ACTIVITIES (Con't)

Objective 9.4: Determine methods of coordinating advertising with other sales promotion activities.

Across

1. combination of methods used by a retailer to communicate with consumers.
3. accumulated and then traded for merchandise or for reductions on groceries.
4. certificate which entitles a person to buy particular offering at a reduced price.
10. free trial products.

Down

1. involves communication from a retailer to consumer.
2. a product or service is given free or at a greatly reduced price with the purchase of another designated offering.
5. an arrangement of merchandise and information for shoppers' viewing.
6. a special arrangement set up beside complete stock of the item.
7. selling of goods at a lower or reduced price for a period of time.
8. a competitive act for increasing sales.
9. special events for demonstrating merchandise.
11. to explain the use of a product or service.
12. free promotion.
13. some stores' very elaborate and expensive supportive promotions.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

INFORMATION SHEET

Objective 9.5: Identify consumer protection laws dealing with advertising.

The small entrepreneur must be more and more concerned with the effect of consumer protection regulations. Regulations on advertising are now being made at Federal, State, and local levels.

Nationally, the Federal Trade Commission, the Food and Drug Administration, and the Federal Communications Commission are among the various regulatory bodies which control the advertising practices of the large corporations. At the retail level are such mechanisms as state departments of consumer affairs, local bureaus of consumer affairs, and the Better Business Bureaus.

Among the regulations of the greatest importance to retailers are those concerning the use of false or misleading advertising resulting in "bait-and-switch" practices. Advertising is a very visible or audible medium, easily subject to supervision and criticism form both legal and consumer standpoints. You should use care in making statements and claims for the products you advertise. Be sure that they conform to the various state and federal regulations and the standards of good taste.

Advertising should be viewed as a sales building investment and not simply as an element of business expense. When it is well planned and well carried out, your advertising can be an important factor in the future growth of your business.

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

QUESTIONS FOR DISCUSSION

Objective 9.5: Identify consumer protection laws dealing with advertising.

A. Of what value to the consumer and the business are the following regulatory bodies:

(1) Federal Trade Commission?

(2) Food and Drug Administration?

(3) Federal Communications Commission?

(4) Better Business Bureau?

UNIT 9.0

BUILDING A FLEXIBLE ADVERTISING PLAN

STUDENT ACTIVITIES

Objective 9.5: Identify consumer protection laws dealing with advertising.

1. Find additional information on any one of the following:
   (a) Federal Trade Commission

   (b) Food and Drug Administration

   (c) Better Business Bureau

2. In addition to the above, find at least one current news article concerning the interaction of government regulation and business in regards to advertising.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

OBJECTIVES

After completing this unit, the student will be able to:

Objective 10.1	Identify the factors that influence the pricing policies of an entrepreneur.
Objective 10.2	List the methods used in the process of determining the price of goods.
Objective 10.3	Describe the pricing procedures used by retailers.
Objective 10.4	Describe a pricing procedure used by manufacturers.
Objective 10.5	Describe the categories of retail credit, the services provided by a credit bureau, and the factors that influence the retailer's decision to offer credit.
Objective 10.6	Define trade credit.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

INFORMATION SHEET

Objective 10.1: Identify the factors that influence the pricing policies of an entrepreneur.

Pricing of goods and services usually includes the cost of goods and services, expenses, and a profit margin. Any business adds value to goods, materials, or supplies. Retailers provide goods and services to the consumer at a convenient location and time; service businesses use suppliers to perform a requested service; wholesalers buy in large quantities and allow smaller quantities to be bought and examined; manufacturers process raw materials. Because of the fact that their business "adds value", they desire to make a profit and must determine a selling price to maximize profits.

The factors that influence pricing policies in addition to costs are:

A. The company policy

B. Nature of the product or service

C. Economics and business conditions

D. Market strategy

E. Competition

F. Methods of distribution

A. Company policy -- Influential factors include: business reputation, customer services offered, location, price reputation (high or low), position in the industry, and expenses.

B. Nature of product or service -- The elasticity or inelasticity of demand on a product or service influences its price. The services of a doctor in an emergency is generally considered to have an inelastic demand as does the purchase of a mink coat. The demand of a washer and dryer is directly related to its price making for an elastic demand. Different products and services carry a varying amount of demand that directly influences the price that will be set.

C. Economics and business conditions -- If economic conditions are good, sellers generally increase their prices to maximize profits. If conditions are poor, the concern is for market share rather than higher price.

D. Market strategy -- Decisions influencing market strategy include:

   1. Low volume, high markup

   2. High volume, low markup

   3. Long run or short run item

E. Competition -- Sellers must look at competition to determine if a competitive price needs to be set. All of the above factors will also influence this decision.

F. Methods of distribution -- Generally distribution costs remain very stable but tend to rise when sales rise.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

QUESTIONS FOR DISCUSSION

Objective 10.1: Identify the factors that influence the pricing policies of an entrepreneur.

A. How can an entrepreneur, in addition to price changes, influence an expansion of the market for the goods or services they offer?

B. Give an example of a product or service and explain how the "nature of" this product influence its selling price.

C. Determine the current economic condition and explain how prices are being influenced at the wholesale and retail levels.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES

Objective 10.1: Identify the factors that influence the pricing policies of an entrepreneur.

1. List 10 products or services in which the demand for these products is inelastic. Explain why for each listed.

2. For your choice of entrepreneurship, how will you determine the most profitable prices?

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

INFORMATION SHEET

Objective 10.2: List the methods used in the process of determining the price of goods.

Below are several different approaches used to determine prices of goods:

A. Full cost pricing -- The price is set to cover the cost of goods sold, all expenses and a percentage of profit already predetermined. This method is considered strict policy, but the entrepreneur can use this method as a base and be flexible with markups.

B. Gross-margin pricing -- Widely used by retailers and wholesalers, this method adds a certain markup to the wholesale cost. The markup will generally vary from product to product and is figured as a percentage of selling price.

C. "Going-rate" prices -- The price of a product is set according to the manufacturers suggested retail price.

D. Marginal-cost pricing -- The relationship of volume, cost and profit is considered with the fixed or variable costs, and price is adjusted according to demand or the market strategy used to sell a product.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

QUESTIONS FOR DISCUSSION

Objective 10.2: List the methods used in the process of determining the price of goods.

A. Why is it necessary for a retailer to maintain pricing policies?

B. Using the marginal cost method, how would a retailer justify selling a product at cost price?

C. How should high fashion goods be priced?

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES

Objective 10.2: List the methods used in the process of determining the price of goods.

Determine the pricing policy you will implement in your business. Justify this method and give examples.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

INFORMATION SHEET

Objective 10.3: Describe the pricing procedures used by retailers.

PRICING AND PRICE CHANGES

Establishing retail prices, maintaining markups and markdowns are the two most important key elements to the retail method of merchandising. Pricing is a topic discussed and varied by many retailers. Individual store pricing policies differ and each company has a set pricing structure. The most common pricing policies are geared toward the psychological attitudes of consumers.

Odd pricing seems to be the most popular, such as $2.99 instead of $3.00. One belief is that prospects perceive odd-ending prices lower than even prices, despite the fact the price difference is very slight. Also, odd point pricing tends to decrease resistance to a price increase. Most retail price decisions are based on judgment, awareness of customer needs, the behavior of competition, and cost and profit goals of the retailer, and trial and error.

Other methods of pricing are as follows:

1. Pricing above the market value: Management charges higher prices without undue regard to customer reaction. (Example: Customer with a high credit risk, specialty item, or no market competition.)
2. Pricing at market level: Majority of retailers offer prices which are competitive with other retailers.
3. Pricing below the market: Discounters retail in this area. Competition is almost the entire reason for low pricing.
4. Pricing private brand: Selling exclusive merchandise to customers who buy only merchandise which they feel is best. (Example: Sears, Wards, Penney's) This method also widens consumer's choice of products they want to purchase.
5. Price Lining: Products or services at a limited number of prices, (Example: $5, $10, and $15) Easier for salespeople and customers to make purchase decisions.
6. Leader Pricing: A low price item which is competitive and placed on sale or priced low to build store traffic, show store is competitive.

Along with pricing, markups and markdowns play an important role in the departments profit margin and department appearance to the customer. Companies have set procedures for markups and markdown merchandise. The form is very specific and is usually handled and repriced by a person from shipping and receiving. Close records must be kept on markups-downs to keep inventory and gross profit margins in line. Markdowns should be taken on:

1. Promotional merchandise which is advertised on sale at a reduced price.

2. Old merchandise which is not selling.

Caution should be used when marking down old merchandise because after a 20% reduction in price, customers have a habit of becoming suspicious of the product. Remember, to keep a balanced inventory, markups should equal or be greater than markdowns.

MARKUPS

The most important formula to remember throughout the unit on markups and markdowns is:

RETAIL = COST + MARKUP

Markup includes the amounts necessary to cover the expenses of operating the business, plus a profit.

Note the abbreviations below:

R = Retail price

C = Cost of merchandise

M = Markup

M% = Markup percentage (based on retail unless otherwise stated)

MR = Markup based on Retail Price

MC = Markup based on Cost of merchandise

It is important to note that percentages can be calculated on either the Retail or Cost. The most common use in retailing is to base markup on RETAIL, thus you may assume that, unless otherwise noted, all markup percents are based on retail. Students should be able to use either type, however.

This unit has four (4) parts:

1. Figuring markup percentage based on RETAIL

2. Figuring markup percentage based on COST
3. Calculating retail price, using Markup on Cost
4. Calculating retail price, using Markup on Retail

1. Figuring markup percentage based on RETAIL:

   GIVEN: The Retail and Cost, Markup and Cost, or Markup and Retail, Calculate the percentage (%) of Markup based on the Retail Price.

   FORMULA: $\text{Markup \% on Retail} = \frac{\text{MARKUP}}{\text{RETAIL}}$ (or) $MR = \frac{M}{R}$

2. Figuring markup percentage based on COST:

   GIVEN: The Retail and Cost, Markup and Cost, or Markup and Retail, Calculate the percentage (%) of Markup based on the Cost of the merchandise.

   FORMULA: $\text{Markup \% on Cost} = \frac{\text{MARKUP}}{\text{COST}}$ (or) $MC = \frac{M}{C}$

3. Calculating retail price, using markup on COST:

   GIVEN: The cost of an item, and the desired markup as a percent of that cost.

   FORMULA: RETAIL = COST + (COST X MARKUP %)

4. Calculating retail price, using markup % on RETAIL:

   GIVEN: The cost of an item, and the desired markup as a percent of the RETAIL price.

   FORMULA: $\text{RETAIL} = \frac{\text{COST}}{(100 - \text{Markup \% on Retail})} \times 100$

MARKDOWNS

A Markdown is any reduction in the retail price, permanent or temporary. Markdowns are usually expressed as a percent of the original retail price, which is deducted to give the reduced retail price.

EXAMPLE:

Lawn mower originally retailed for $149.95

End-of-Season Close-out sale, all prices reduced 25%

$149.95	(Original Retail)
x .25	(Markdown percent)
74975	
29990	
374875	= 37.4875, or $37.49

$149.95	(Original Retail)
less 37.49	(Markdown amount)
$112.46	(Reduced Retail Price)

CLOSE-OUT PRICE = $112.46

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

QUESTIONS FOR DISCUSSION

Objective 10.3: Describe the pricing procedures used by retailers.

A. What psychological effect can prices have on customers?

B. How can discount stores price below the going market?

C. When should markdowns be taken?

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES

Objective 10.3: Describe the pricing procedures used by retailers.

LIST AND IDENTIFY

1. List and describe seven pricing methods.

   (a)

   (b)

   (c)

   (d)

   (e)

   (f)

   (g)

2. Markdowns should be taken on:

   (a)

   (b)

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES (con't)

Objective 10.3: Describe the pricing procedures used by retailers.

3. Compute the retail price for the merchandise items listed below. Use the markup percent given.

(a) COST = $4.95; Markup % = 66% on Cost RETAIL = ______________

(b) COST = $19.75; Markup % = 75% on Cost RETAIL = ______________

(c) COST = $39.50; Markup % = 38% on Retail RETAIL = ______________

(d) COST = $150.00; Markup % = 44% on Retail RETAIL = ______________

4. INSTRUCTIONS: In the "Given" column below, fill in any blanks. Then calculate the percent of markup on both RETAIL and COST, and write those answers in the correct areas. Round all percents to NEAREST WHOLE PERCENT.

	GIVENS					PERCENT OF MARKUP	
	RETAIL	=	COST	+	MARKUP	ON COST	ON RETAIL
(a)	$ 1.00		$ .80		$______	___________	___________
(b)	3.75		______		.95	___________	___________
(c)	4.50		2.75		______	___________	___________
(d)	______		4.60		1.30	___________	___________

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

INFORMATION SHEET

Objective 10.4: Describe a pricing procedure used by manufacturers.

WHAT IS THE BEST SELLING PRICE?*

The "best" price for a product is not necessarily the price that will sell the most units. Nor is it always the price that will bring in the greatest number of sales dollars. Rather the "best" price is one that will maximize the profits of the company.

The "best" selling price should be cost oriented and market oriented. It should be high enough to cover your costs and help you make a profit. It should also be low enough to attract customers and build sales volume.

A Four Layer Cake

In determining the best selling price, think of price as being like a four layer cake. The four elements in your price are: (1) direct costs, (2) manufacturing overhead, (3) nonmanufacturing overhead, and (4) profit.

Direct costs are fairly easy to keep in mind. They are the cost of the material and the direct labor required to make a new product. You have these costs for the new product only when you make it.

On the other hand, even if you don't make the new product, you have manufacturing overhead such as janitor service, depreciation of machinery, and building repairs, which must be charged to old products. Similarly, nonmanufacturing overhead such as selling and administrative expenses (including your salary) must be charged to your old products.

Direct Costing

The direct costing approach to pricing enables you to start with known figures when you determine the price for a new product. For example, suppose that you are considering a price for a new product whose direct costs -- material and direct labor -- are $3. Suppose further that you set the price at $5. The difference ($5 minus $3 = $2) is "contribution." For each unit sold, $2 will be available to help absorb your manufacturing overhead and your nonmanufacturing overhead and to contribute toward profit.

*Source: "What is the Best Selling Price?" (Washington, D.C.: Small Business Administration), Small Business Administration Management Aid No. 193.

Price-Volume Relationship

Any price above $3 will make some contribution toward your overhead costs which are already there whether or not you bring the new product to market. The amount of contribution will depend on the selling price which you select and on the number of units that you sell at that price. Look for a few moments at some figures which illustrate this price-volume-contribution relationship:

Selling price	$5	$4	$4
Projected sales in units	10,000	30,000	15,000
Projected dollar sales	$50,000	$120,000	$60,000
Direct costs ($3 per unit)	$30,000	$ 90,000	$45,000
Contribution	$20,000	$ 30,000	$15,000

In this example, the $4 selling price, assuming that you can sell 30,000 units would be the "best price" for your product. However, if you could sell only 15,000 units at $4, the best price would be $5. The $5 selling price would bring in a $20,000 contribution against the $15,000 contribution from 15,000 units at $4.

With these facts in mind, you can use a market-oriented approach to set your selling price. Your aim is to determine the combination of selling price and unit volume which will provide the greatest contribution toward your manufacturing overhead, nonmanufacturing overhead, and profit.

Complications

If you ran a nonmanufacturing company and could get as much of a product as you could sell, using the direct costing technique to determine your selling price would be fairly easy. Your success would depend on how well you could project unit sales volume at varying selling prices.

However, in a manufacturing company, various factors complicate the setting of a price. Usually, the quantity of a product that you can manufacture in a given time is limited. Also whether you ship directly to customers or manufacture for inventory has a bearing on your production and financial operation. Sometimes your production may be limited by manpower. Sometimes by equipment. Sometimes by the availability of raw materials. And sometimes by practices of your competition. You have to recognize such factors in order to maximize your profits.

The direct costing concept enables you to key your pricing formula to that particular resource -- manpower, equipment, or material -- which is in the shortest supply.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

QUESTIONS FOR DISCUSSION

Objective 10.4: Describe a pricing procedure used by manufacturers.

A. How do marketing costs affect the pricing policies of manufacturers?

B. What is nonmanufacturing overhead? Give examples.

C. Explain -- "The best price for a product is not necessarily the price that will sell the most units."

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES

Objective 10.4: Describe a pricing procedure used by manufacturers.

1. List six factors that can complicate the setting of a price for a manufacturer.

   (a)

   (b)

   (c)

   (d)

   (e)

   (f)

2. List and define the four elements that make up a manufacturer's pricing structure.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

INFORMATION SHEET

Objective 10.5: Describe the categories of retail credit, the services provided by a credit bureau, and the factors that influence the retailer's decision to offer credit.

RETAIL CREDIT AND COLLECTIONS*

Retail credit is a part of everyday living in America. Retailers sell on credit and buy on credit from their suppliers who, in turn, order on credit from the companies who manufacture the merchandise. Many of their customers rely on credit because it allows them to buy what they want, when they want it, and to pay for it from future earnings. This wide use of credit in the Nation's economic system helps to maintain a balance between production, distribution, and consumption of goods.

Categories of Consumer Credit

Consumer credit is divided into two categories, namely, purchase credit and loan credit. The consumer uses purchase credit to acquire merchandise from retail stores or to obtain services of various kinds. He uses loan credit to borrow from banks, finance companies, credit unions, savings and loan associations, and other kinds of lenders.

Purchase credit -- There are several types of purchase credit offered by retailers. The title affixed to each type may vary, but basically they are variations of the charge account, or ordinary open account, in which the customer arranges for credit service on a short-term basis of usually 30 days. This is generally thought of as a cash transaction where the credit privilege is offered as a convenience to the customer.

By the late 1920's, retail credit began to be recognized as a sales tool to increase store volume. To meet the demands of customers for big ticket merchandise, retailers started to use the installment credit purchase account more extensively. Under this plan, purchase arrangements were set forth in a contract, usually a conditional sales contract. Such contracts allow consumers to have use of some durable goods while paying for the items over a given number of months. A service charge is added to cover the costs of extending this privilege.

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*Source: "Retail Credit and Collections" (Washington, D.C.: Small Business Administration), Small Business Bibliography No. 31.

As the use of retail credit widened, credit managers developed further variations of the ordinary open account. The budget account, for instance, allows the consumer to purchase goods and pay for them over a specified number of months in regular installments. A charge is made for the credit service and a downpayment is required. In another variation, the revolving account, a fixed amount of credit is predetermined by the customer and the credit manager. The customer usually pays nothing down in advance, since no debt is incurred until a purchase is made. The advantage of this type of account is that it allows the consumer to purchase needs up to the ceiling. At the end of the month, the customer pays an agreed amount on the account, say one-sixth if the account is for 6 months' duration. The customer is then in an open-to-buy position and can purchase again until the ceiling is reached. A service charge is made for this convenience.

The term option account, a third variation, has become common in retailing. This is a combination of the open account and the revolving account. Under this plan, the customer may pay in full when billed at the end of the month, or elect to make a partial payment and carry the balance over to the succeeding month. Thus, the customer pays a service charge only if the revolving account plan is used. The charge is made only on the amount carried forward.

Loan credit -- While loan credit is not granted by retailers, consumers use it to purchase merchandise from them. In the past, these loans were obtained mainly for the liquidation of indebtedness to retailers and others. By consolidating many obligations into one debt, the consumer can make smaller payments to one financial institution and eventually work his/her way toward solvency.

This use, although still prevalent, has given way to other reasons for borrowing cash. Today, the consumer frequently borrows to take advantage of needs, such as vacations and education. Many times, the consumer has investments which are earning interest or dividends and does not want to disturb them. He/she would prefer using this investment as security and borrow against it. Through disciplining himself/herself, he/she meets his/her new installment obligations and at the same time preserves his/her initial investment.

Credit Reporting Services

One reason that the extension of credit to the consumer has been so successful can be traced to the unique service of the credit bureau. This organization, located in the business community, collects pertinent data on citizens living in the trading area who use credit. Businesses which have need for the service belong to the credit bureau and help to keep the files current by recording their customer experience in this depository. For the customer who has a good credit record, and this constitutes 95 percent of the purchasers, credit extension is an almost routine matter.

Consumer credit reporting is international in scope. Through membership in the Associated Credit Bureaus, Inc., the local credit bureau manager has available to him current file information in some 2,500 credit bureaus in the United States, Canada, and other countries. Should a consumer move, he/she can request that his/her credit record be sent to the credit bureau in the new community in advance so that he/she will have credit readily available upon his/her arrival. Through the medium of electronics, local credit bureaus will shortly be tied into a network so that information on any consumer can be made available at a moment's notice.

Should a Retailer Offer Credit?

This is a question which the retailer will have to decide for himself/herself. His/her decision will depend largely upon what his/her competition is doing. Business survival is dependent upon meeting competition and making a profit.

In some lines of retail business, credit service is a must. This applies to durable as well as nondurable goods. Especially when a product carries a manufacturer's suggested sales price, the merchant who does not offer credit service is at a decided sales disadvantage.

Providing retail credit, requires considerably more cash than is necessary in a cash-and-carry business. The cost of merchandise -- not to mention the profit -- is not returned to the credit retailer for at least one month and, in some instances not for 1 to 3 years. As an example, under certain conditions it is estimated that a merchant will need $33,390 to carry installment sales credit amounting to $10,000 a month. However, the additional income produced through a service charge will eventually warrant the extra cost of offering credit. Then, too, the offering of credit generates additional sales.

Of course, the extension of credit has its disadvantages, especially if the customer fails to repay in full. An inexperienced credit granter can make mistakes in judgment and put unprofitable business on the books. For some firms, accounts receivable represent 50 to 75 percent of the firm's assets. When collections begin to fall off on these accounts receivable, capital reserves must be drawn upon in order to continue in business. Attempts to recover unpaid accounts through professional collectors may help, if placed in time. Unfortunately, as the accounts receivable age, chances for collection decline rapidly.

Should a Retailer Have His/Her Own Credit Department?

Most retailers prefer to conduct their own credit departments. They believe there is a great deal of store loyalty generated through credit service. Whether customers come in to pay their accounts, or simply mail their checks in payment, merchants know that customers shop more regularly where they have credit accounts.

Retailers tend to look upon credit customers as repeat business and cash customers as one timers. This is not necessarily true, but it does have some merit. Credit customers also tend to spend more than cash customers. The credit department is no longer considered a nonproductive department because it generates sales and produces income from service charges. Retail management now allocates large budgets to the credit sales departments and gives its credit executive a say in management decisions.

A great many retailers delegate the management of their credit departments to local and national credit card and charge plans. These plans also give retailers access to a larger number of potential credit customers than they would have if they ran their own credit departments. They also relieve the merchant from onerous paperwork, the need for capital to finance receivables, and the necessity of hiring specialized credit employees. For a small percent of the sales check, the specialized plan takes over the credit functions of the retailer, usually on a nonrecourse basis. It leaves the retailer free to concentrate on increasing his/her sales volume. He/she must, however, continue to keep up with the changes taking place in the consumer credit industry. Should he/she ever decide to leave the community plan, he/she may need to organize his/her own credit department.

The Federal Consumer Credit Law

On May 29, 1968, the President of the United States signed into law a Federal regulatory law known as the Consumer Credit Protection Act of 1968. Consumer credit transactions between sellers and lenders and the vast number of buyers and borrowers are regulated by the Act which became effective as of July 1, 1969. In addition to containing truth-in-lending features, the Act applies to credit advertising, wage garnishments, and extortionate credit transactions. The law is administered through the Board of Governors of the Federal Reserve System and eight other Federal agencies.

Data Processing in Credit

Recent developments in electronic data processing are being applied to the field of retailing and credit reporting. The retail credit and collection departments have welcomed this development because it speeds up the processing of vast amounts of paperwork, gives the credit manager a daily readout on the volume of credit sales and payments on account, and shows up delinquent accounts before they have a chance to age.

The adaption of data processing to the consumer credit industry is in its infancy. In the years immediately ahead, there will be a movement toward the automation of credit offices in the small and medium-sized retail stores, either through specialized service agencies, banks, or pooling through a businss community cooperative association.

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

QUESTIONS FOR DISCUSSION

Objective 10.5: Describe the categories of retail credit, the services provided by a credit bureau, and the factors that influence the retailer's decision to offer credit.

A. What are the advantages and disadvantages of offering credit to customers?

CREDIT TO CUSTOMERS

ADVANTAGES	DISADVANTAGES

B. What services do credit bureaus provide for businesses?

C. Describe the Truth In Lending law. Who benefits from this law?

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES

Objective 10.5: Describe the categories of retail credit, the services provided by a credit bureau, and the factors that influence the retailer's decision to offer credit.

Go to a local retail store and obtain a credit application. Actually apply for credit at that particular store to discover either how difficult or easy it is to obtain consumer credit. Notice the questions that are being asked of the applicant. Why are such questions asked? Did you feel the application was too personal? Who do you think your application was approved (or disapproved)?

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

INFORMATION SHEET

Objective 10.6: Define trade credit.

A. Trade credit -- Trade credit, also referred to as mercantile or commercial credit, is credit extended by one business to another to help the sale of production or commercial goods. It is sometimes considered less of a lending method and more of a means of simplifying payment of goods. Usually the account is paid within 30 days of the invoice date. Discounts are offered to encourage earlier payment and are known as trade credit terms.

B. Trade credit application -- Information should be gathered on a busines much like the information you might obtain from a customer for a retail store. The following information should be obtained:

1. Name of business
2. Address
3. Type of business
4. Other credit accounts
5. Number of years in business
6. Financial and bank references

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

QUESTIONS FOR DISCUSSION

Objective 10.6: Define trade credit.

A. Which do you think is easier to obtain, trade credit or retail credit? Why?

B. Why do you think discounts are used to encourage a business to pay a bill within 30 days?

C. Do you think most businesses adhere to a strict trade credit policy? Why might this policy be flexible?

UNIT 10.0

DETERMINING PRICING AND CREDIT POLICIES

STUDENT ACTIVITIES

Objective 10.6: Define trade credit.

1. List and define various trade credit terms offered by businesses.

2. Define:

    (a) Extra Dating

    (b) Seasonal Dating

UNIT 11.0

INVENTORY AND SUPPLIES

OBJECTIVES

After completing this unit, the student will be able to:

Objective 11.1	Identify the types of supply sources.
Objective 11.2	Develop company policies and procedures for buying.
Objective 11.3	Determine factors that influence buying decisions.
Objective 11.4	Describe methods of stock control.
Objective 11.5	Determine a plan of maintaining complete stock assortments.

UNIT 11.0

INVENTORY AND SUPPLIES

INFORMATION SHEET

Objective 11.1: Identify the types of supply sources.

SUPPLY SOURCES

Various terms are used to describe where the entrepreneur obtains his/her goods. Sources of supply, vendor, resource, and supplies, are all terms that imply a source of goods.

There exists two main classes of merchandise or supply resources: (1) the manufacturer, and (2) the middleman.

Manufacturer: The entrepreneur deals directly with the producer or manufacturers. The manufacturers provides company representatives that are well informed on consumer demands and trends.

Some of the advantages of buying directly from the manufacturer are:

1. The merchandise can be produced and packaged to meet the business' request.
2. There is less delivery time loss when the manufacturer sells directly to the business.
3. The entrepreneurs take on the function of middlemen so they can experience a reduction in price.
4. Usually service is taken care of quickly.

Middlemen: This person is between the manufacturer and business. There are two main types of middlemen.

A. Agent Middleman: He/She does not take title to the goods. They negotiate purchases for the business or represent the producer.

B. Merchant Middlemen:

   1. Wholesaler -- They buy from manufacturers and resell to retailers. They take title to the goods, store the goods, and assume all risks.
   2. Full Service Wholesaler -- Extend credit and other services to the business.
   3. Limited Function Wholesaler -- Do not extend many services, but do perform supplier services.

Some of the advantages of buying from middlemen are:

1. If a variety of goods are needed, it is easier to deal with a few wholesalers than a lot of manufacturers.
2. Location of the middleman is generally more convenient than a manufacturer.
3. Can usually buy in smaller quantities.
4. The wholesaler usually provides more services than a manufacturer.

THE BUYING OFFICE

Most large businesses have a resident buyer that goes out into the market to visit suppliers, examine the goods, obtain price quotes, and gather terms, etc. It is not always possible to have a resident buyer that can always be in the market. Therefore, the business could be represented by a buying office, usually located in the market. These offices maintain a staff that keeps up to date on resources and trends in the market.

The business pays a fee to the buying office and in turn the buying office provides such services as announcements of new products, information on the best selling items, market data and forecasts, help in developing buying plans, and help in solving problems after orders have been completed.

MANUFACTURER'S REPRESENTATIVES

Manufacturer's representatives furnish a great deal of usable information to the buyer. This information includes facts on marketing, product information, merchandising, and even consumer information.

Many times they can furnish dealers' aids and tie-in advertising. They may furnish newspaper clippings, TV spots, and radio advertising that promote the product. The manufacturer may pay for some of these.

From what the manufacturer's representatives see in other businesses, they may tell the buyer of other successful marketing procedures. Sometimes they can assist in training the sales force.

Manufacturer's representatives can assist the entrepreneur on what quantities to buy. In some cases, they set racks, count the stock, and prepare orders for additional quantities. They also know price laws and regulations.

Manufacturers often have information on new products, such as results of laboratory tests. This is made available to buyers.

Often times the manufacturer's representative can furnish information on transportation and handling charges. One merchant who could not compete on a seasonal item was informed of drop shipments that helped bring transportation costs down. With this, the business was able to undersell the competition and also increase the turnover of an item the store needed to carry.

Manufacturer's representatives see a number of businesses selling a given item. Sometimes they can pass on pricing policies they have seen that increase turnover or profit margins. Effective product display ideas from the same source may also be passed on to the buyer.

Storing or warehousing of some products may be improved sometimes as a result of suggestions from manufacturer's representatives. They see and can tell of improved handling procedures, combining storage, and displays.

Consumers are increasingly protected by laws and regulations. Manufacturer's representatives can help the entrepreneur keep up to date on them.

Manufacturer's representatives also have or know about consumer surveys. They can pass on this information. Some of it may be drawn from consumer research carried on by the manufacturer or trade associations. Some may be from the company's experience with consumers in its distribution area. This information may be of the following nature:

1. Style information, as in clothing, automobiles, etc.
2. Package preferences of customers, including brand image
3. Consumer reaction to various kinds of display or advertising
4. Kinds of guarantees consumers prefer. . .or accept
5. Credit and refund policies that consumers choose
6. Seasonal merchandise preferences of customers
7. Customer reactions to special promotions, such as premiums, trading stamps, and others
8. Consumer reactions to pricing policies
9. Success of consumer panels and other forms of consumer participation

UNIT 11.0

INVENTORY AND SUPPLIES

QUESTIONS FOR DISCUSSION

Objective 11.1: Identify the types of supply sources.

A. What advantages might the entrepreneur experience when buying directly from the manufacturer?

B. What services are provided by a buying office? Would it be advantageous for a small business to secure the services of a buying office?

C. How important are manufacturers representatives to a:

(1) Small Business?

(2) Large Business?

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES

Objective 11.1: Identify the types of supply sources.

Contact a buying office that might possibly supply your type of business. Make a list of all services that office would supply you, the entrepreneur. Include the cost of such a service. Then determine if such a service would be feasible for your business.

UNIT 11.0

INVENTORY AND SUPPLIES

INFORMATION SHEET

Objective 11.2: Develop company policies and procedures for buying.

COMPANY POLICIES AND PROCEDURES FOR BUYING

An entrepreneur usually has developed policies and practices in order to effectively manage those activities related to its goals. A firm that is managed by sound policies that follow government regulations, is sure to meet its goals while maintaining a good market reputation.

When policies are established to manage daily decision making, two major purposes are met: (1) Efficiency and profits are improved by eliminating inconsistencies; (2) That consistency maintains a good market reputation for the business that is a priceless asset when working with customers and resources.

There are as many reasons for establishing policies as there are business firms. The merchandising policies are usually the most important policies that are set up in a retail store. Generally, these policies serve as guidelines in purchasing and as a means of control in stock· inventories. Some of the most typical of firm's merchandising policies deal with the following general areas:

A. Business Image

B. Qualities and Values of Products or Services

C. Complete Assortments

D. Merchandising by Classification and Price Ranges

E. Investments

F. Purchase Discounts

G. Markdowns

H. Competition

Another policy area is that of dealing with resources. It is to the advantage of both buyer and seller to maintain a fair, honest, and ethical relationship in order to maximize their profits. The consumer needs to be considered in this relationship since they ultimately pay the price of the merchandise.

As stated earlier, a good market reputation is a priceless asset in the marketplace. Most of the trade practices that are followed by the buyer and seller are connected to the purchase order which is a legal and binding contract. A fair and respectable relationship must remain intact while negotiating this type of business.

It is the buyer's responsibility to get the best possible price and terms for the goods or supplies being purchased. It is the seller's responsibility to get the goods or supplies to the buyer as the buyer has ordered and at the time requested.

Although profits depend on quick decisions, a greater loss could occur if these same decisions are not made with sound policies and restrictions.

UNIT 11.0

INVENTORY AND SUPPLIES

QUESTIONS FOR DISCUSSION

Objective 11.2: Develop company policies and procedures for buying.

A. What is the relationship between sound company policies and company goals?

B. Discuss -- "A good market reputation for a business is a priceless asset when working with customers and resources."

UNIT 11.0

INVENTORY AND SUPPLIES

QUESTIONS FOR DISCUSSION (Con't)

Objective 11.2: Develop company policies and procedures for buying.

C. Discuss the advantages and disadvantages of using a single supply source.

SINGLE SUPPLY SOURCE

ADVANTAGES	DISADVANTAGES

D. How do policies and procedures protect the:

(1) Buyer?

(2) Entrepreneur?

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES

Objective 11.2: Develop company policies and procedures for buying.

1. Select a business and interview management.

2. If possible, obtain a written statement of resource policies.

3. Present your findings to the class or submit a written report to the instructor.

UNIT 11.0

INVENTORY AND SUPPLIES

INFORMATION SHEET

Objective 11.3: Determine factors that influence buying decisions.

COMPETITIVE BIDS

Buyers have to be able to understand and negotiate various prices and terms that are offered by the resources. The buyer is faced with obtaining the best goods or supplies that can be sold favorably and still yield a profit to the business. If more than one resource carries a product or supply , the buyer may ask each of the resources to submit a best offer. That offer should include the price of the product or supply along with related services such as transportation terms, discounts, delivery schedules, credit, advertising aids, and other possible terms. From this information, or bid, the buyer compares the different offers to determine which resource could provide the company with the best price and terms.

Generally, it is more important to buy the right goods from the right resource than to save a few pennies. Successful buyers are "shrewd traders." If a fair price is offered they usually accept, but if the buyer feels a better price can be obtained, an attempt to negotiate for a better price is made.

TERMS OF AN ORDER BILLING AND SHIPPING MERCHANDISE

Different manufacturers or resources have their own conditions or terms of an order. Before signing an order, buyers must know what discounts they may receive, what method of dating will be used, and what transportation arrangements are to take place.

DEFINITIONS

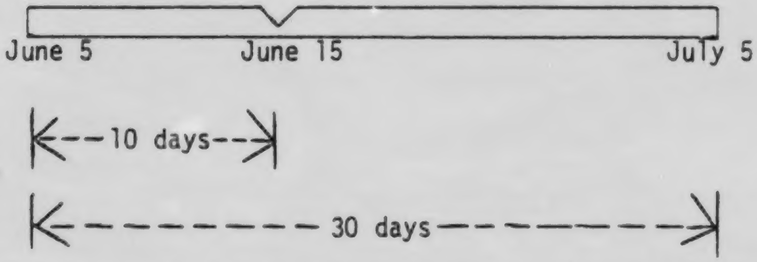
I. Discounts: A reduction in the price of merchandise is made. Five different discounts will be discussed: Cash Discount, Anticipation Discount, Trade Discount, Quantity Discount, and Promotional Discount.

A. Cash Discount: A cash discount is given if the buyer pays within specified period of time after the date of the invoice (bill). Most sellers offer a cash discount in order to induce the buyer to pay in advance of the final due date. This type of discount is usually expressed in the form "3/10, net 30," meaning a 3 percent discount may be taken up to the tenth day after the invoice date (3/10). If the invoice is not paid within the 10 days, then the total net amount is due 30 days after the invoice date (net 30). For example: You ordered a quantity of goods costing $800, your invoice date was June 5th, and your cash discount terms were 2/10, net 30. What is the latest date that you can still experience the 2% discount? When is the net amount due?

1. Period during which 2% discount can be taken

Period during which net amount must be paid.

The latest date for the 2% discount is 10 days past June 5th (invoice date) which is June 15.



2. The net amount is due 30 days past the invoice date which is July 5th. How do you figure a cash discount? If you pay within the discount period, you must multiply the amount of the discount by the amount of the invoice. This will give you a dollar amount of the discount. Subtract the dollar amount of the discount from the total amount of the invoice and the amount is what is owed. Using the above example: $800 invoice, terms: 2/10, net 30.

Paying within the
discount period
between June 5
and 15.

$800.00 = Invoice
x .02 = 2/10=2% Discount in 10 days
2% expressed as a decimal=.02
16.0000 = Amount of discount

800.00 = Invoice
- 16.00 = Discount
784.00 = Amount of Invoice Experiencing the Cash Discount

B. Anticipation Discount: If a buyer pays before the end of the cash discount, the buyer is sometimes able to take a discount in addition to the cash discount. This is called an anticipated discount. Buyers deduct interest, often at a rate of 6% a year, for the number of days of prepayment.

If terms were 2/15, net 30 with a net amount of $1000, payment 5 days after the invoice date would earn a 2% cash discount. The invoice date would be $980. If the accepted rate of interest is 6%, then an additional 1.63 would be deducted (6% on $980 for 10 days).

Invoice -	$1000	$1000.00
Discount Rate -	X.02	- 20.00
Amount of Discount	$20.00	$980.00

C. Trade Discount: This is a method of quoting prices based on list prices. Businesses are often given a stated trade discount, for example, 40%, off of the list price.

List price - $2.00
Less 40% - .80
Amount of Item - 1.20

D. Quantity Discount: This is a discount given usually on large orders. For example, there may be no quantity discount on orders under 500 cases of an item, a 2% discount on orders of 500-1000, a 3% discount on orders of 1000-1500 etc.

E. Promotional Discount: This discount is intended to repay the buyer for advertising the resource's or seller's product. Generally it is at a rate of 1, 2, or 3 percent.

II. Dating: This is the time the buyer is given to pay his bill. There are several variations.

A. COD: Cash on Delivery -- The buyer pays cash for the goods when they are delivered.

B. EOM: End of Month -- When the date of an invoice is figured from the end of the month. If goods are shipped March 5th, they do not have to be paid for until a specified number of days after the end of the month.

C. MOM: Middle of the Month -- Any invoice dated between the 1st and 15th is considered dated the 15th. Invoices dated between the 15th and the end of the month are considered dated the end of the month.

D. ROG: Receipt of Goods -- The date of payment is computed from the date the goods are received by the buyer rather than the invoice date.

E. Extra Dating: The buyer is given extra days in which to pay. This is used to encourage buyers to buy early. Extra dating is usually expressed by an X followed by the number of days allowed.

Terms 6/10, net 30, X 60

Invoice date March 14

The 6% discount could be taken to May 26 with net due June 15th.

III. Transportation: "How are the good shipped?" "Who is going to pay for them?" "Who is to own the goods while in transit?" These are all questions to the buyer. The terms of shipment indicate when the title to the merchandise goes from seller to buyer and who is to pay for the cost of transportation.

A. FOB Origin: Free on board, from origin. The title of the goods goes to the buyer when the seller gives the goods to the carrier at the departure point (origin). All transportation charges expenses and risks are the responsibility of the buyer from then on.

B. FOB Destination: Seller pays transportation and assumes the responsibility for expenses and risks of transportation. Title goes to the buyer when the merchandise is delivered to the destination point.

C. FOB Origin Freight Allowed: The business may deduct the transportation cost from the invoice. Title and responsibility go to the buyer when the seller gives the goods to the carrier.

D. FOB Origin, Freight Prepaid: Seller pays the cost of transportation. Title goes to buyer when goods are given to carrier at point of origin.

E. FOB Destination, Charges Reversed: Seller pays transportation costs and assumes responsibility for expenses and risks of transportation, but the cost is later paid back to the seller by the buyer.

UNIT 11.0

INVENTORY AND SUPPLIES

QUESTIONS FOR DISCUSSION

Objective 11.3: Determine factors that influence buying decisions.

A. Discuss - "Generally it is more important to buy the right goods from the right resource than to save a few pennies."

B. Discuss - "Successful buyers are 'shrewd traders.'"

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES

Objective 11.3: Determine factors that influence buying decisions.

1. Discounts and Dating

(a) Amount of invoice-$700.00 Date of invoice-October 16 Terms-3/10, n/45, MOM

By what date would the invoice need to be paid to earn the discount? __________________. How much would be paid if the discount were taken?____________________. When is the net amount of the invoice due?___________________________.

(b) Amount of invoice-$680.40 Date of invoice-January 11 Terms-2/15, n/45,X 30

If anticipation is taken at 6% how much would be due on the invoice if paid on January 11?______________________. If the invoice were paid on January 16 how much would the payment be?_________________.
When is the net amount of the invoice due?________________________.

2. Comparison of Offers

(a) Product-Tennis shoes-Need-12 dozen in full range of sizes and assorted colors.

Supplier A-Cost per dozen-$21.60 Terms-8/10, n/60

Supplier B-Cost per dozen-$22.80 Terms-8/10, n/60, 2% extra on all

Supplier C-Cost per dozen-$22.10 Terms-8/10, n/60, 1% extra on full cost of any orders over 9 dozen

Which supplier has the lowest overall cost?________________________

Which supplier would have the lowest cost on an order of 24 dozen?

___________________________________.

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES (con't)

Objective 11.3: Determine factors that influence buying decisions.

2. (b) Product-Screwdriver sets, 1/2 inch drive 18 piece

Vendor A-Cost per set-$17.00 Terms-2/10, n/30, X 30

Vendor B-Cost per set-$16.50 Terms-2/10, n/60

Vendor C-Cost per set-$16.90 Terms-2/10, n/45, MOM (invoice date would be June 18)

Which supplier has the lowest price?______________________________.

If you wishes to delay payment as long as possible which supplier should be used?______________________________.

If Vendor A offered a 2% promotional and Vendor C offered a 1% promotional would this change the vendor with the lowest price?______.

If you were presently stocking tools from Vendor A why would you consider buying from either Vendor B or C?______________________________.

3. Transportation Terms

(a) Pat's Camping Supplies ordered 50 tents from the Joe's Tent Company.

The terms of the sales were as follows: Amount of invoice-$2,716.00

Date of invoice-February 20 Terms-2/20,n/90 Freight-$136.30,

F.O.B.-Origin-Freight Allowed.

Who is to pay the freight costs on this order?____________________.

When does Pat's Camping Supplies take title to the tents?________

______________________________.

What is the amount of payment on this invoice if paid March 15?

______________________________.

What is the net amount of this invoice?__________. When is it due?______________________________.

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES (con't)

Objective 11.3: Determine factors that influence buying decisions.

3. (b) Pat's Men's Store placed an order with Smith's Coat Company for 150 golf jackets. The terms of the order were as follows: Amount of invoice-$1,350.00 Date of invoice-March 20 Terms-6/10, n/30, Freight-$24.60 F.O.B.-Destination-Charges Reversed.

Who is to pay the freight costs of this order?__________________.

When does Pat's Men's Store take title to the jackets?__________

____.

What is the amount of payment on this invoice if paid March 26?

____.

What is the amount of payment on this invoice if paid April 20?

____.

UNIT 11.0

INVENTORY AND SUPPLIES

INFORMATION SHEET

Objective 11.4: Describe methods of stock control.*

Maintaining effective control over stock is important in all kinds and sizes of business operations, but it can be critical in a small one. At best, the owner-manager of a small store flirts with loss when he/she lets his/her stock become unbalanced.

The type of merchandise you handle will largely determine the kind and amount of paperwork needed for effective stock control. For example, control of perishables -- such as in a delicatessen -- requires no paperwork. Stocks are controlled visually. Many deliveries -- such as milk and bread -- are daily, and others are frequent. In addition, the suppliers' routemen have a self-interest in helping keep stocks fresh.

But even so, the owner-manager may need some sort of reminder -- perhaps a note on his/her calendar -- so he/she can make periodic checks. The important thing is to watch for changing customer demands requiring changes in your purchases.

The situation is different, though, with parts inventory in a service operation and with sizes and styles in an apparel store. For example, the owner-manager of a shop that specializes in motor tuneup and speedometer repair work may keep track of some of the parts he/she uses every day with little effort. But what about those he/she uses only once a month? Some sort of record is necessary if the right parts are to be on hand when he/she needs them.

In shoes, ladies ready-to-wear, and other soft goods stores, style, color and sizes complicate the problem of stock control. A great deal of paper work may be necessary in order to serve customers properly and to prevent over or underbuying.

Stock control is necessary if the entrepreneur is to offer his/her customers a balanced assortment. A system need not be elaborate. It should enable the entrepreneur to determine what needs to be ordered on the basis of: (1) what is on hand, (2) what is on order, and (3) what has been sold.

The Basic Picture

The owner-manager of almost any small business can sketch the basic picture of stock control. It involves four facts: (1) what you have on hand, (2) what you have on order, (3) what you have sold, and (4) what you need to order.

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*Adapted from "Stock Control For Small Stores" (Washington, D.C.: Small Business Administration), Small Marketers Aid No. 123.

But whether these facts are used to achieve effective control is another story. A memory lapse on any of them can mean being out of stock or overstocked on an item, a style, a color, or a size.

What Kind of Records?

Stock control records help prevent memory lapses. They eliminate the need for carrying details -- especially on styles, colors, and sizes -- in one's head, a trying task. They provide a container into which the owner-manager can deposit details.

The kinds and number of control records which an owner-manager uses depend on the amount of details that are needed. Stock control system may be achieved either by counting stock or by counting sales. Either way, a model stock list is required.

The Model Stock List

A model stock list is the first step in setting up a replenishment system for merchandise that involves styles, colors, and sizes. You prepare a list of all the items you want to control.

The list should include "model stock" quantities. These quantities are the amounts needed in order to maintain an "in stock" position for a certain period -- usually a number of weeks.

You can use a simple formula to determine the period of time to be covered by the model quantity. It is: Reorder Period + Delivery Period = Number of Weeks.

Counting Stocks or Sales?

Counting is the basis for getting the information necessary to effective control. You can count stock on a periodic basis or you can count it daily by counting sales.

Which is best for your situation depends on the kind of merchandise you carry and the amount of work involved for you and your salespeople. Your goal should be to use a method which will provide up-to-date information at the most economical cost.

If You Count Stock

Your situation may lend itself to counting the stock on a periodic basis. If so, you would use what is called "the rotated method" and record the information on cards.

In the rotated method of stock control, you use rotated unit control cards. The format varies according to the kind of merchandise, but the kind of information is the same. With such a card, you keep track of an item, such as shoes by listing: (1) what is on hand, (2) what is ordered, (3) what has been received, and (4) what has been sold. Once every 2 weeks, the stock is counted to determine how well an item sold is selling.

If sales are dragging, you may decide to close out the item. If sales are normal, you would order the normal fill-ins. On the other hand, the stock count and other information on the card may reveal that sales are greater than activity on the sales floor has indicated. If so, your decision may be to increase the filling order and plan to promote the item.

The principle behind the rotated method is: Old Inventory + Purchases - New Inventory = Sales. In this formula, you can substitute the word "disappearance" for the word "sales." Disappearance represents shoplifting inaccuracies in counting inventory, and sales.

If You Count Sales

The other method for controlling stock is the perpetual method. In it, stocks are calculated from the store's recorded sales.

If you use this method, you have to keep track of sales when they are made, on an item basis. Its usefulness depends on whether the device you use captures the information with a minimum of effort and chance for error. The owner-manager with a fairly large sales volume (some experts say $200,000 annually) should check the possibility of using a computer service center to count sales and create up-to-date stock records. Such data processing may be more economical than maintaining the records manually.

Even when electronic data processing is not used, cash register tape may be such a device for capturing the needed information. If a sales count is needed on only a few items, you could check the possibility of using your register to get the information. For example, "Key A" might stand for one item number, "B" for another, and so on.

Sales slips provide another device for recording the item sales. Still another is the price ticket which can be detached when the item is sold.

Whether the information comes from register tape, sales slips, or price tickets, it has to be related to your stocks, specifically to particular classes of merchandise. A drug store, for example, needs sales information on prescriptions, proprietaries, fountain, sundries, tobacco, confections, magazines, and toiletries. The best way is to summarize the information and post it daily to your stock records.

These up-to-date stock records provide the information you need for ordering fill-ins. You review them on a periodic basis -- once every 2 weeks, for example -- and reorder as needed. One disadvantage is that errors can creep into the posting of the daily sales. However, adjustments can be made through a physical count of stocks every so often.

If you have only one or two items that need unit control, you might want to work with price tickets. At the time of the sale, detach the ticket and file it for later posting on your record. The balance on hand after posting will determine what you need to reorder.

The principle behind the perpetual method is: Old Inventory + Purchases - Sales = New Inventory.

Preventing Excess Stocks

In a small business, preventing excess stock serves two purposes. One is the maintenance of a balanced assortment which allows the business to serve customers. The other is the assurance that an excessive amount of working capital is not tied up in merchandise or supplies.

Open-to-buy is the key to keeping stocks in line. Open-to-buy is the amount of merchandise (in units or dollars) that you need to receive into stock during a certain period.

The period may be the selling season that is customary for a certain line of merchandise. Or it may be a time-span that is set by the owner-manager to fit his particular situation.

A side benefit from stock control records is that they are helpful in delegating work. They provide concrete tools which you can use in training an employee to care for details, such as counting stock.

UNIT 11.0

INVENTORY AND SUPPLIES

QUESTIONS FOR DISCUSSION

Objective 11.4: Describe methods of stock control.

A. What is the objective of stock control?

B. Define:

(1) Model Stock List

(2) Perpetual Stock Control

(3) Open to Buy

C. What is the difference between basic stock and model stock?

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES

Objective 11.4: Describe methods of stock control.

Set up a stock control system for the business you are about to open. Summarize the main points of your control system and submit a written report to your instructor.

UNIT 11.0

INVENTORY AND SUPPLIES

INFORMATION SHEET

Objective 11.5: Determine a plan of maintaining complete stock assortments.

MERCHANDISE PLANNING

The purpose of the merchandise plan is to realize a net profit from the department at the end of the year through careful planning, paying close attention to past successes and failures.

Merchandise planning is necessary for all stores, whether large or small. Even though the small store does not need as elaborate a plan as the larger store, a plan is necessary in order to help eliminate problems such as overbuying.

DETERMINING THE PLAN

Many considerations are necessary in determining the merchandise plan, such as:

1. Figures from the Previous Year, Including Sales, Stocks, Purchases, Markups, etc.
2. Figures From a Recent Month
3. Economic Condition, Including Employment, Prices, and Market Activity
4. Changes in Styles
5. Transportation Condition and Time Necessary for Deliveries
6. Competition
7. Market Conditions for Particular Merchandise
8. Needs for Special Purchases or Seasonal Differences
9. Special Department Problems
10. Growth of the Department or Store

Because merchandising involves purchasing in advance and must be based on some estimate, a well-researched plan is quite valuable. Planning ahead (forecasting) intelligently helps make it easier to handle sudden changes. A good plan must anticipate probable future changes.

Because the image of the store or department is based on merchandise assortment, control is vital. This assortment and control is based on customer needs. Since the objective of stock planning is to maintain an inventory that is balanced according to the needs and wants of customers. The total stock should be sufficient to meet reasonable demand and still allow for rapid turnover. Factors which need to be considered are store experience, order time, etc.

Each department needs a merchandise plan covering a six-month period and based on sufficient stock to allow for planned sales. This plan must also be in keeping with total store budget. It must allow for purchases, mark-ups, markdown, etc. and should be completed at least two months before the beginning of the period.

Be using last year's figures for the same period and then considering current changes, the buyer is able to determine realistic goals. Current changes may include:

1. Sales -- a regular monthly increase of 20% will indicate that it is safe to forecast a continuing monthly increase of 20%.

2. Stock -- based on basic assortment of stock required, promotional merchandise, type of department, price lines to be increased, and desirable turnover.

While some stores use the turnover basis for arriving at stock figures, others use the Stock-Sales ratio, and some use both systems. The Stock-Sales ratio is determined by dividing the stock at the beginning of each month by the sales volume figure for that month. The major advantage of this method is that monthly variations show up more noticeably.

The merchandise plan based on customer wants and needs provides the buyer with the background necessary to buy the proper types of goods within a certain amount of money. In order to determine the proper quantity, the buyer must look for items that will provide rapid turnover, decrease markdowns, attract many customers, and return a reasonable profit.

For basic stock, the proper quantity depends on the following:

1. Expected Sales -- This is determined by looking at the sales for the same period over several past years and adding the increased volume.

2. Turnover -- Refers to the number of times the stock has been sold in a given period of time.

3. Location of Buying Source -- The closer the sources, the less need to buy large stocks.

4. Style Trends -- If the merchandise is a "fad", perishable, etc., special care must be exercised not to overbuy.

5. Projected Supply and Prices -- If it appears that there will be no difficulty in obtaining the item later, then there is less need to place a large order.

6. Credit -- The policies of the company with which the buyer is dealing will determine in part the quantity of merchandise purchased.

7. Service -- The buyer will need to consider the convenience to the customer. If additional parts must also be purchased in order to insure quality service, this will determine in part how much of an item to stock.

8. Display Needs -- Displays are most effective in selling merchandise, and here must be an adequate supply to allow for display.

9. Attractiveness -- The quantity which allows for the most effective presentation to the customer should be purchased.

   Example: Children's shorts-$3.99 per pair or two pairs for $6.00.

ANALYSIS OF MERCHANDISE PLAN

1. The past records of the previous year are recorded, (sales, stocks, purchases, expenses, and markup).

2. Sales are planned. Sales are planned before other factors because they depend so much on outside conditions. It is easier to adjust stocks, markups, and expenses to sales possibilities than it is to plan these factors and then try to reach a sales goal consistent with them.

3. The next step is to plan the amount of stock to have on hand at the first of each month.

4. Planned purchases may be calculated by using this formula:

   Planned purchases + Planned Sales = Increase (or Decrease) in Inventory.

Example:	Department R -	Planned Sales - March 1	$10,000
		Planned Stock - March 1	16,900
		Planned Stock - April 1	17,000
		Planned increase in inventory	100

   Put this in the formula: $10,000 Planned Sales
   100 Increase in Inventory
   $10,100 Planned Purchases

5. Expenses are planned next. Salaries represent the largest total item of expense. It is to be expected that the total expenses will increase with an increase in sales. Salaries, advertising, and other expenses all are increased in the plan because of the planned increase in sales. Outside economic factors must also be considered.

6. Markup is usually set for the entire season rather than being set separately for each month.

TERMS TO CONSIDER FOR KEEPING INVENTORY CURRENT

1. Delivery Period -- The time interval between placing an order and having the merchandise on hand ready for sale

2. Re-order Period -- The weeks or months during which re-orders should be placed

3. Normal Sales Expectancy -- The number of units of merchandise to be sold during a certain period

4. Safety Factor -- The amount of stock needed to avoid being "out of stock" in the delivery and re-order period

5. Merchandise on Order -- Merchandise ordered but not received

6. Stock on hand -- Current inventory in store

UNIT 11.0

INVENTORY AND SUPPLIES

QUESTIONS FOR DISCUSSION

Objective 11.5: Determine a plan of maintaining complete stock assortments.

A. Why is merchandise planning necessary? What are its objectives?

B. How can one estimate the expected sales for a particular period?

C. Is it better to have a high turnover or low turnover of your product?

UNIT 11.0

INVENTORY AND SUPPLIES

STUDENT ACTIVITIES

Objective 11.5: Determine a plan of maintaining complete stock assortments.

You are the merchandise manager in a small department store. One of your department managers comes to you with a request to re-order some merchandise that has been selling well. Following each of the steps below, you are to write a brief explanation of how that item will affect your decision to place a re-order.

Interview a merchandise manager or buyer to help determine how each will affect your decision to place a re-order.

1. Delivery Period:

2. Re-order Period:

3. Normal Sales Expectancy During the Above 2 Periods:

4. Safety Factor Desired:

5. Stock on Hand:

6. Merchandise on Order:

7. Vendor's Minimum Shipping Quantity:

8. Other Items to be Considered:

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

OBJECTIVES

After completing this unit, the student will be able to:

Objective 12.1	Determine the importance of a good accounting system.
Objective 12.2	Understand the basic accounting components for starting a business.
Objective 12.3	Develop a cash budget.
Objective 12.4	Understand the importance of an Income Statement.
Objective 12.5	Understand the importance of a Balance Sheet.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

INFORMATION SHEET

Objective 12.1: Determine the importance of a good accounting system.

A. An effective accounting system is essential to efficient management of business affairs.

B. An accounting system is made up of many functions which include the following:

1. Provides information relative to the financial position of the business
2. Provides information concerning the profitability of the business
3. Provides information for the preparation of tax returns
4. Provides information for effective planning and control

C. Small businesses need an accurate and up-to-date account of all transactions affecting the business.

D. Each business transaction is identified, recorded, and summarized in order to provide the information for periodic reports used by the owner or other decision makers.

E. An effective accounting system provides the information needed for external accounting requirements. These external parties include customers (accounts receivable), creditors (accounts payable), banks (loans), employees (payroll), and government (taxes).

F. An effective accounting system provides information needed for internal accounting requirements. This information serves as a stimulus for decision making.

G. A major factor for the failure of at least 90% of the businesses is due to a lack of adequate accounting records.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

QUESTIONS FOR DISCUSSION

Objective 12.1: Determine the importance of a good accounting system.

A. How do good accounting records increase the chances of staying in business?

B. If you are a customer, supplier, employee or government agency representative, what accounting information would you need for each situation?

C. As a business owner, what accounting information would you require to make decisions affecting your business?

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES

Objective 12.1: Determine the importance of a good accounting system.

1. Talk to five small business owners and ask them why their accounting records are so important. Compare your findings with classmates.

2. Visit a small business and find out what special accounting information is used by their customers, creditors, banks, employees and government.

3. Choose your favorite small business and determine what accounting information would be needed to make a decision of renting or purchasing equipment.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

INFORMATION SHEET

Objective 12.2: Understand the basic accounting components for starting a business.

A. The types of accounting records which are needed in starting a business are as follows:

1. Cash Receipts
2. Cash Disbursements
3. Sales
4. Purchases
5. Payroll
6. Equipment
7. Inventory
8. Accounts Receivable
9. Accounts Payable

B. The general journal and general ledger are books of original entry and final entry or book of accounts respectively. Each business transaction should be analyzed and recorded in the general journal. After all the transactions for a day or week have been recorded, they are posted or transferred to the general ledger. The information in the general ledger is used to prepare the financial statements.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

QUESTIONS FOR DISCUSSION

Objective 12.2: Understand the basic accounting components for starting a business.

A. From the nine basic types of accounting records needed in a business, which records should be maintained daily, weekly, monthly, etc? Why?

B. What is an example of a transaction that should be recorded in a general journal? Why is it important to record this information in the general journal? Why should you not record it directly in the general ledger?

C. Why is it important to be aware of the tax considerations of a business? Should you just let your accountant worry about it? What happens if you keep your own records?

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES

Objective 12.2: Understand the basic accounting components for starting a business.

1. For each of the nine basic accounting records, prepare an actual record and list the type of information that would be included in each one.

2. Although you would need to take an accounting principles course to learn the basic rules for double-entry accounting, list the types of resources you can consult to help you understand this information.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES (Con't)

Objective 12.2: Understand the basic accounting components of starting a business.

3. Call or visit the various tax offices and accumulate the types of forms, instructions, etc., for each item. Compare your materials with others in the class.

4. Show a free Internal Revenue Service film for small businesses entitled, "Hey, We're in Business!" After viewing the film, ask the students to identify areas that the small business owner did not take into consideration when starting and operating the business.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

INFORMATION SHEET

Objective 12.3: Develop a cash budget.

A. A cash budget helps you see the dollar amount of your expenses you will be incurring each month matched with the projected cash budget. It is a management tool which helps to determine the times during the year which your business may encounter reduced sales and needed additional cash requirements. In other words, it is a plan expressed in financial form.

B. In establishing a cash budget, the first thing to consider is estimating your fixed and controllable (or flexible) expenses for each month of the year.

C. After determining the expenses (including the start-up expenses), you should determine the estimated cash requirements for each month of the year. Remember that sometimes your business may need more money in addition to normal sales because adequate working capital is necessary for success in your business.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

QUESTIONS FOR DISCUSSION

Objective 12.3: Develop a cash budget.

A. Why is it so important that a small business develop and maintain a cash budget?

B. In determining your monthly expense requirements, what are the expenses that would be classified as start-up, fixed and controllable (or flexible) in a small business? Where can you get industry percentages? See Barometer of Small Business.

C. After you have determined your monthly expense requirements, you have a good idea of the minimum amount of cash needed each month. What are the ways an individual business owner can generate cash?

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES

Objective 12.3: Develop a cash budget.

1. Develop a list of advantages and disadvantages of having a cash budget. Compare your list with others in the class.

2. Visit local small businesses and ask the owners the types of expenses they incur both fixed and controllable. Also, ask the owners, in addition to sales, where do they generate additional cash requirements. Compare answers with students who interviewed the same or different types of businesses.

3. In a small group, assume you were asked as consultants to help develop a cash budget for a small business, list the steps you follow to complete the budget.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

INFORMATION SHEET

Objective 12.4: Understand the importance of an Income Statement.

A. An Income Statement reflects the operations of a business by showing the income or loss for a period of time. It is like a motion picture which shows the revenues and expenses over a particular period of time.

B. An Income Statement for a small business generally includes the following categories:

Net Sales		$100,000
Cost of Goods Sold:		
Beginning Inventory	$30,000	
Purchases	+40,000	
Goods Available for Sale	$70,000	
Ending Inventory	-20,000	
Cost of Goods Sold		-50,000
Gross Profit or Margin		50,000
Operating Expenses:		
Rent	$ 1,000	
Salaries	5,000	
Utilities	500	
Depreciation	+ 1,500	
Total Operating Expenses		-8,000
Net Income		$42,000

C. An Income Statement may reveal various items that need looking into. Comparing your figures with prior year statements can indicate trends. Also, comparing your figures with other firms in your line of business can help identify trouble spots.

D. An owner of a business should pay close attention to the cost of goods sold because usually this cost is the highest cost a business incurs.

E. A general definition for costs and expenses is the outflow of resources or the incurring of a debt for goods or services rendered to the business in order to generate revenue. One expense that does not require a physical outflow of resources is depreciation. This expense represents a reduction in the book value of the asset.

Discussion Overhead for Objective 12.4

FUN FASHIONS
Balance Sheet
As of December 31, 1978

Net Sales		$100,000
Cost of Goods Sold:		
Beginning Inventory	$30,000	
Purchases	+40,000	
Goods Available for Sale	$70,000	
Ending Inventory	-20,000	
Cost of Goods Sold		-50,000
Gross Profit or Margin		50,000
Operating Expenses:		
Rent	$ 1,000	
Salaries	5,000	
Utilities	500	
Depreciation	+ 1,500	
Total Operating Expenses		-8,000
Net Income		$42,000

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

QUESTIONS FOR DISCUSSION

Objective 12.4: Understand the importance of an Income Statement.

A. "How much profit are we making?" and "Where is all the money going?" are two important questions asked by business owners. What do these two questions mean to you?

B. What basic information is included on an Income Statement?

C. In comparing your Income Statement figures with prior years or with other firms in your type of business, what can you benefit by this procedure? What specific areas would you look at first? Can this information help you make any decisions in the future?

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES

Objective 12.4: Understand the importance of an Income Statement.

1. Go to at least three small businesses in your neighborhood and ask the owner-manager(s) how important an Income Statement is to them. Compare findings with classmates.

2. Assume that you bought a used bicycle for $40 and you decided to fix it up to sell. You spent a total of $10 for repair expenses and $2 for an ad in a local newspaper. You sold the bicycle for $75. How much money did you make? From the preceding information, show similarities between this information and an actual Income Statement of a small business.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES (Con't)

Objective 12.4: Understand the importance of an Income Statement.

3. From the following information, prepare an Income Statement for the period ending December 31, 1979: Sales, $100,000; Beginning Inventory, $25,000; Purchases, $65,000; Ending Inventory, $35,000; Depreciation -- Office Equipment, $1,000; Salary Expense, $10,000; Advertising Expense, $2,000; Rent Expense, $1,500; Miscellaneous Expenses, $3,000.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

INFORMATION SHEET

Objective 12.5: Understand the importance of a Balance Sheet.

A. A Balance Sheet shows the financial position of a business for a particular date. It is like a snapshot of the business showing the assets (owned by the business), liabilities (owed by the business), and owner's equity (owner's claim against the assets or the owner's net worth or interest).

B. A Balance Sheet for a small business generally include the following categories:

Current Assets			Current Liabilities	
Cash		$15,000	Accounts Payable	$ 5,000
Accounts Receivable		8,000	Short-Term Loans	10,000
Merchandise Inventory		5,000		
			Long-Term Liabilities	
Fixed Assets			Long-Term Loans	20,000
Building (if owned)	$42,000		Mortgage	+30,000
less accumulated dep'n	(2,000)	40,000		
Land (if owned)		20,000	Total Liabilities	$65,000
Equipment	$14,000			
less accumulated dep'n	(4,000)	10,000	Owner's Equity or Net Worth	+33,000
Total Assets		$98,000	Total Liabilities and Owner's Equity	$98,000

C. A relationship exists between the fundamental accounting equation (Assets = Liabilities + Owner's Equity) and the Balance Sheet.

Discussion Overhead for Objective 12.5

FUN FASHIONS
Income Statement
for the Year Ended December 31, 1978

Current Assets			Current Liabilities	
Cash		$15,000	Accounts Payable	$ 5,000
Accounts Receivable		8,000	Short-Term Loans	10,000
Merchandise Inventory		5,000	Long-Term Liabilities	
Fixed Assets			Long-Term Loans	20,000
Building (if owned)	$42,000		Mortgage	+30,000
less accumulated dep'n	(2,000)	40,000		
Land (if owned)		20,000	Total Liabilities	$65,000
Equipment	$14,000		Owner's Equity or Net Worth	+33,000
less accumulated dep'n	(4,000)	10,000		
Total Assets		$98,000	Total Liabilities and Owner's Equity	$98,000

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

QUESTIONS FOR DISCUSSION

Objective 12.5: Understand the importance of a Balance Sheet.

A. A Balance Sheet contains three major categories. Name and explain what they are and give examples of each.

B. What is meant by a Balance Sheet being referred to as a snapshot of the business? What value does this statement have for the business?

C. Who besides the owner of the business may be interested in the Balance Sheet? What influence does the Income Statement have on a Balance Sheet? Which should be prepared first?

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES

Objective 12.5: Understand the importance of a Balance Sheet.

1. Go to the library and find three Balance Sheets from three different types of businesses. List the similarities and the differences.

2. Assume that you want to find out your own personal net worth. List all the items you own (e.g., car, bicycle, radio, clothes, etc.) and list all the items that you owe (e.g., amount owed on car or bicycle, money you borrowed from a friend, etc.) From this information can you determine your net worth? Show similarities between this information and a Balance Sheet from a small business.

UNIT 12.0

UNDERSTANDING A BASIC ACCOUNTING SYSTEM

STUDENT ACTIVITIES (Con't)

Objective 12.5: Understand the importance of a Balance Sheet.

3. From the following information, prepare a Balance Sheet as of December 31, 1979: Cash, $5,000; Accounts Receivable, $2,000; Merchandise Inventory, $5,000; Equipment, $15,000; Accounts Payable, $3,000; Notes Payable, $2,000; Mortgage Payable, $10,000; Owner's Equity, $12,000.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

OBJECTIVES

After completing this unit, the student will be able to:

Objective 13.1	Identify the major types of insurance for a small business.
Objective 13.2	Determine the outcomes of having an effective insurance plan.
Objective 13.3	Determine what to look for in evaluating an insurance company.
Objective 13.4	Determine what to look for in evaluating an insurance agent.
Objective 13.5	Understand the importance of an effective security system.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

INFORMATION SHEET

Objective 13.1: Identify the major types of insurance for a small business.

A. Fire Insurance -- Insures the small businesses from loss due to fire, lightning, and removal of goods from the premises because of fire.

B. Liability Insurance -- Is probably one of the most important forms of insurance a small business should carry. It insures the small business from judgments brought against the business because of bodily injury and/or property damage as a result of negligence. Also, a small business may purchase liability insurance to cover against business operation losses. One should note that most small businesses are either sole proprietorships or partnerships and the owners have unlimited liability. In other words, the owner is liable not only the extent of his/her investment but also, if needed, to the extent of the owner's personal assets.

C. Workmen's Compensation -- A state mandated program which requires that the small business provide benefits to employees injured at work. Generally the state laws determine the types of payment made to employees and their dependents.

D. Fidelity Bonds -- Guarantees that your employees are honest in carrying out their work obligations and protects the employer from losses due to dishonesty of the bonded employee. Normally, any employee having access to business funds should be bonded.

E. Business Interruption Insurance -- Insures the small business by compensating for the costs incurred because of the business being shut down as a result of a power failure, fire, or other damages.

F. Crime Insurance -- Compensation for the losses of the business because of burglary, theft, or robbery.

G. Business Life Insurance -- Insures the small business owner for a number of purposes. Some of these purposes are as follows:

   1. Sole Proprietorship Insurance -- Provides for the maintenance of the business upon the death of the owner.

   2. Partnership Insurance -- Provides for the retirement of partner's interest upon death.

   3. Corporation Insurance -- Provides for the retirement of the shareholder's interest upon death.

4. Key-Man Insurance Protection -- Provides for the loss as a result of the death of a key employee.

5. Small Business can provide or help provide group life and health insurance, group annuity, pension plans, or individual retirement policies.

H. Automobile Insurance -- Is a form of liability and property insurance. Based on the type of coverage, this policy insures the small business owner against such things as collision, theft, fire, and glass breakage. Also, the owner can have coverage when an employee or subcontractor uses their own car on behalf of the small business owner.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION

Objective 13.1: Identify the major types of insurance for a small business.

A. What are the purposes of the following types of insurance policies?

(1) Fire

(2) Liability

(3) Workman's Compensation

(4) Fidelity Bonds

(5) Business Interruption Insurance

(6) Crime Insurance

(7) Business Life Insurance

(8) Automobile

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION (Con't)

Objective 13.1: Identify the major types of insurance for a small business.

B. What are the advantages and disadvantages of having the preceding types of insurance?

FIRE

ADVANTAGES	DISADVANTAGES

LIABILITY

ADVANTAGES	DISADVANTAGES

WORKMAN'S COMPENSATION

ADVANTAGES	DISADVANTAGES

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION (Con't)

Objective 13.1: Identify the major types of insurance for a small business.

B. (Con't)

FIDELITY BONDS

ADVANTAGES	DISADVANTAGES

BUSINESS INTERRUPTION INSURANCE

ADVANTAGES	DISADVANTAGES

CRIME INSURANCE

ADVANTAGES	DISADVANTAGES

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION (Con't)

Objective 13.1: Identify the major types of insurance for a small business.

B. (Con't)

BUSINESS LIFE INSURANCE

ADVANTAGES	DISADVANTAGES

AUTOMOBILE

ADVANTAGES	DISADVANTAGES

C. Of the eight previous types of insurance, which one is the most important? Why? Which one is the least important? Why?

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

STUDENT ACTIVITIES

Objective 13.1: Identify the major types of insurance for a small business.

1. In addition to the eight types of insurance mentioned in this unit, list any other types of insurance a small business might purchase.

2. Choose one or two of the types of insurance you have listed and write to an insurance company for information on those types of insurance policies. Compare findings with classmates.

3. Visit a local small business and find out what types of insurance policies the owner has. Determine if the policies are different from your list. If there are some differences, try to list the reasons why the particular type of business may have a different policy.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

INFORMATION SHEET

Objective 13.2: Determine the outcomes of having an effective insurance plan.

A. Insurance provides protection for the owner of a small business against serious losses.

B. A small business owner needs to make certain that insurance covers every angle of the business. One should recognize the various ways loss can be incurred.

C. Some insurance plans, such as business life insurance, will provide a reserve for emergencies. Most of these plans have cash value and can be used as collateral for loans made to the business.

D. An effective insurance program, in addition to providing protection against losses, can also provide such things as ease of obtaining credit, loss prevention, freeing money for investments by building the present and future security of the business, and the owner's family and owner's peace of mind.

E. A sound insurance protection plan is as important to the success of a small business as sound marketing, accounting, financing, etc., plans. This plan is achieved through good planning and organization.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION

Objective 13.2: Determine the outcomes of having an effective insurance plan.

A. What does a small businessperson consider as the most important factor for purchasing insurance? Why?

B. Is it necessary for a small business to insure that all possible losses will be covered? Why? What alternatives should be considered?

C. Should insurance be considered as a resort in a small business? Why?

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

STUDENT ACTIVITIES

Objective 13.2: Determine the outcomes of having an effective insurance plan.

1. List as many possible benefits or values a small business can be provided through insurance.

2. Call an insurance company and find out what the insurance company thinks is the prime benefit of having insurance for a small business.

3. Ask your parents or guardians about their insurance coverage. Determine if there are any similarities between their insurance coverage and a small business. List them.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

INFORMATION SHEET

Objective 13.3: Determine what to look for in evaluating an insurance company.

A. When evaluating a potential insurer, the first thing a small business owner should do is to review the financial stability of the company. By consulting the evaluations of Alfred M. Best Company in most public or college libraries, one can determine the financial strength as well as the efficiency of management and operations. Many of these areas are rated in order to help in the evaluation of the insurance companies.

B. The insurer's field of specialization should be considered. Specialization in certain types of coverage will provide a small business owner an important advantage of experience in dealing with unique insurance consideration.

C. A key characteristic a small business owner should look for in the flexibility of adapting the insurer's policies to the individual needs of the small business. Various provisions can be incorporated into the insurance contract.

D. Another area that should be considered is the cost of the coverage. One should not confuse the terminology used when dealing with premium amounts. For example, the initial premium payment should not be compared with the actual net premium payment. One should seek advice from specialists in the field.

E. An additional area to consider when choosing an insurance company is its claim services. The quick reaction time of the company regarding a claim is of utmost importance to many small businesses. Perhaps one should contact some policyholders of the companies under consideration and determine the efficiency of the service.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION

Objective 13.3: Determine what to look for in evaluating an insurance company.

A. From the five criteria for evaluating an insurance company, which criterion is the most important? Why?

B. Why is it so important for a small business owner to research various insurance companies before purchasing insurance? How can the owner secure the necessary information to evaluate the insurance companies?

C. An important factor in the success of a small business is an effective insurance plan. What value can an insurance company provide in developing a plan? Should the small business owner seek input from other companies regarding the insurance plan?

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

STUDENT ACTIVITIES

Objective 13.3: Determine what to look for in evaluating an insurance company.

1. List as many insurance companies you possibly can; then consult a phone book or other reference and add to your list.

2. From your list of companies, contact three and ask them to quote the insurance premium for a type of insurance a small business would need. Compare findings with classmates.

3. Contact three local businesses and ask the owners what insurance company provides their coverage and why they chose the particular company. Compare findings with classmates.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

INFORMATION SHEET

Objective 13.4: Determine what to look for in evaluating an insurance agent.

A. Probably one of the most important factors in buying insurance is the selection of an insurance agent.

B. One criterion in evaluating an insurance agent is the agent's contacts among the various insurers. The agent's contact should be broad enough to supply the small business owner the proper insurance coverage and at a reasonable cost.

C. The insurance agent should have a thorough knowledge of all the facets concerning insurance. One way of identifying the agent's knowledge and professionalism is the agent's possession of Chartered Life Underwriter (CLU) or Chartered Property and Casualty Underwriter (CPCU) designations.

D. The insurance agent should be able to provide the small business owner a degree of individual attention. The agent should be a friend; one who can be trusted and is helpful in devoting enough time and energy to the small business owner's individual insurance problems.

E. An area which also should be considered in evaluating an insurance agent is the quality of extra services provided to the small business owner. The agent should not just collect premiums but to counsel the owner regarding effective and proper insurance and loss-prevention programs. The agent should also help evaluate various alternative methods of insurance coverage.

F. The insurance agent should be available to help in a time of loss. Proper service during this time is extremely important and should be identified in the evaluation of the agent.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION

Objective 13.4: Determine what to look for in evaluating an insurance agent.

A. From the five basic criteria in evaluating an insurance agent, discuss the one criterion you feel is the most important. How would you rank the other four? Why?

B. Why is it important to evaluate prospective insurance agents? What value does it serve? Who benefits from this evaluation? Why?

C. Discuss -- "Better agents usually represent better companies."

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

STUDENT ACTIVITIES

Objective 13.4: Determine what to look for in evaluating an insurance agent.

1. List as many services an insurance agent can provide a small business owner. Compare list with classmates.

2. Interview two insurance agents who deal in small business coverage and list the services they provide. Compare findings with classmates.

3. Contact two small businesses in your local area. Ask them if they deal with only one agent. If they do, ask them why. Compare findings with classmates.

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

INFORMATION SHEET

Objective 13.5: Understand the importance of an effective security system.

A. Employee theft accounts for about two-thirds of total theft in retail organizations.

B. Although a small business owner cannot eliminate stealing entirely, the owner can take steps to minimize it by prevention. These steps are as follows:

1. Improve the level of personnel by carefully screening applicants; setting a tone or atmosphere which encourages honesty; and provide incentives by matching each individual to the right job, set clear lines of authority and responsibility, and remove the temptation to steal.

2. Awareness of theft hazards. Some of these hazards and remedies are as follows:

    a. Pricing Procedures

        1. Price Items by Machine or Rubber Stamp and not by Handwriting

        2. Permit Only Authorized Employees to Set Prices and Mark Merchandise

        3. Make Unannounced Spot Checks to be Sure That Actual Prices Agree With Authorized Prices

    b. Refunding Procedures

        1. Insist on a Merchandise Inspection by Someone Other Than the Person Who Made the Sale

        2. Match Items to the Return Vouchers and Then Return the Merchandise Back Into Stock as Quickly as Possible

        3. Keep a Tight Control on All Credit Documents -- Spot check customers by mail or telephone to make sure they got their refunds

    c. Cash Handling

        1. Pay Special Attention to Cashiers When They are Surrounded by Clusters of People

        2. Be Alert to the Use of Over-Ring Slips to Cover Up Shortage
        3. Watch for Items Bypassed when Ringing up Sales

    d. Backdoor Thefts

        1. Have a Secondary Check by a Worker on all Incoming Shipments
        2. Prohibit Employees From Parking Near Receiving Door
        3. Keep Receiving Door Locked When Not in Use

C. Shoplifting is more prevalent in self-service types of businesses.

D. A small business owner cannot eliminate shoplifting entirely; however, just like employee thefts, one can minimize it by prevention. Some actions to take the reduce shoplifting are as follows:

    1. Keep Tight Checks and Controls on Washrooms and Fitting Rooms
    2. Keep Unused Checkout Aisles Closed
    3. Schedule Working Hours to Assure Adequate Personnel Coverage During Peak Periods
    4. Keep Doors That are Used Infrequently Locked
    5. Keep Small Expensive Items in Locked Display Cabinets
    6. Display Small Inexpensive Items Behind the Checkout Counter
    7. Make Sure Employees Know What to do When They Spot a Shoplifter

E. Burglary is any unlawful entry to commit a felony or a theft, even though no force was used to gain entrance.

F. Prevention must start with the small business owner, and the owner can take measures to protect the business from burglars. Some of these measures are as follows:

    1. Install Suitable Locks -- Most experts agree that the pin-tumbler cyclinder lock provides the best security.
    2. Install an Appropriate Alarm System -- A silent control-station burglary alarm system provides the business the best protection.
    3. Install Adequate Indoor and Outdoor Lighting.
    4. Purchase a Secure Store Safe -- The Small business owner should have a strong safe which deters burglars. Locate the safe so that it is visible to the outside street and well-lighted all night.

G. Robbery is stealing or taking anything of value by force, or violence, or by use of fear.

H. Just like employee theft, shoplifting, and burglary, prevention is the best way to minimize the losses. As a small business owner, some precautions to take are as follows:

1. Train Employees on How to Act and What to Look For During a Holdup
2. Don't Build up Cash on Hand -- Keep as little cash as possible in the store.
3. Develop an Opening and Closing Routine -- Opening and closing a business should be a two person job.
4. Be Cautious on Night Calls

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

QUESTIONS FOR DISCUSSION

Objective 13.5: Understand the importance of an effective security system.

A. Why is employee theft a problem in small businesses? What can a small business owner do to minimize it?

B. Shoplifting is a common problem among small businesses. Name and discuss five ways to reduce shoplifting.

(1)

(2)

(3)

(4)

(5)

C. Why is prevention so important in reducing losses from:

(1) Employee Theft?

(2) Shoplifting?

(3) Burglary?

(4) Robbery?

UNIT 13.0

SELECTION OF EFFECTIVE PROTECTIVE STEPS

STUDENT ACTIVITIES

Objective 13.5: Understand the importance of an effective security system.

1. A small business owner can get advice, assistance, and information regarding the four areas covered in this unit from a merchants' protective association, retail credit bureau, better business bureau, police department, and the district attorney's office. Contact one of these information sources and determine what information it can provide a small business.

2. Visit three local small businesses and identify by observation the ways the small businesses are preventing loss through a security system. Compare findings with classmates.

3. Interview one small business owner and determine what measures the owner takes to overcome these problems.

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